No._____

Supreme Court, U.S.
FILED

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CLERK

In The Supreme Court Of The United States

OCTOBER TERM, 1998

DOMINICK LaROSA and
CATHERINE LaROSA,

Petitioners,

vs.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. May the Internal Revenue Service, which issued a refund of interest to Petitioners, be equitably estopped by its actions from suing Petitioners two years later to recover that refund, where the refund had been authorized by the highest IRS official in the IRS District and the traditional elements of estoppel are present?

2. Is the Internal Revenue Service required to stop the running of interest on an assessed tax liability as of the date the IRS seizes cash sufficient to satisfy the assessment, even where the IRS and the taxpayer purport to agree to hold that cash in "escrow"?

PARTIES

The names of the parties are stated in the caption.

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PETITION FOR A WRIT OF CERTIORARI

Dominick LaRosa and Catherine LaRosa hereby petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case.

OPINIONS BELOW

The Per Curiam opinion of the court of appeals (App., infra, Item 2) is officially reported at 155 F.3d 562 (Table). The opinion of the District Court (App., infra, Item 3) is reported at 993 F. Supp. 907 (D. Md. 1997).

JURISDICTION

The judgment of the court of appeals was entered on July 10, 1998. A timely petition and suggestion for rehearing en banc were denied on September 8, 1998. App., infra, Item 1. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

The pertinent sections of the Internal Revenue Code

of 1986 (26 U.S.C.)*, are set forth in the Appendix, at Item 4.

STATEMENT OF THE CASE

1. This case concerns the availability and scope of the equitable doctrine of estoppel as applied in cases involving actions of Internal Revenue Service officers and agents. That doctrine holds that, under some circumstances, a party may be estopped by its conduct from suing to collect an alleged prior debt where the circumstances showed the party reasonably relied to his detriment on the other party's actions or statements, was unaware of any error, and it would be unconscionable not to grant equitable relief. See Saltzman, IRS Practice and Procedure (Warren, Gorham & Lamont, 1981), Section 3.04[9], citing and summarizing cases.. In this case, the Internal Revenue Service (through the Department of Justice) sued the Defendants/Petitioners, Dominick LaRosa and Catherine LaRosa, to recover an "erroneous refund" (26 USC §7405) two years after the IRS had issued that

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* All references are to the Internal Revenue Code of 1986 ("IRC"), unless otherwise states.

refund and had apologized in writing for its own error in failing to grant it earlier. (App. Item 5, infra).* Whether the Internal Revenue Service may be equitably estopped under any circumstances, and in particular under the circumstances of this case (see below), has bedeviled the Courts of Appeals for at least 30 years without definitive guidance from this Court. Indeed, at least two Courts of Appeal themselves acknowledge the confusion as to the scope of this doctrine in federal tax cases.

2. This case also concerns the proper interpretation of Sections 6335, 6342, 7406 and 7809 of the Internal Revenue Code of 1986 (IRC), and related statutes, which detail the duty of the Internal Revenue Service to collect cash, apply the cash to pay tax assessments, and by that application, stop the running of interest on the taxes. For example, IRC §6342, entitled "Application of Proceeds of Levy" describes the duty of the IRS to apply seized

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* The authority of the IRS to recover an "erroneous refund" under IRC Sec. 7405 is legally distinct and irrelevant to the IRS' authority to audit a return and propose more taxes. The IRS is always free to audit (within the period of limitations) and propose more taxes, even where it had previously issued a refund. That process does not make the prior refund "erroneous." The Section 7405 action is for other errors (including computational errors), not for additional taxes resulting from audits.

funds in a certain sequence, including the tax liability of the taxpayer. Section 7809 requires that tax collections be made and credited daily.

BACKGROUND

3. During the 1970s, Dominick LaRosa, his brother Joseph and their father Pietro, were shareholders of The LaRosa's International Fuel Company, Inc., an "S" corporation for tax purposes. The father and two sons had formed this corporation, after working for years in the coal fields of West Virginia, to take advantage of the fact that the family had negotiated several multi-million dollar contracts with West Virginia utility companies to supply coal. The corporation serviced those contracts through the mid 1980's.

4. Beginning in 1979, the corporation elected the "completed contract" method of accounting on its federal income tax returns to report the income generated by the utility contracts. This method permits the reporting of income for tax purposes when a contract is completed, rather than when payments are received, generally in a year later than would otherwise be the case. It was, in part, a dispute over the entitlement to the completed contract

method of accounting that resulted in the eventual tax assessments and refunds at issue.

5. Some time before December 3, 1985, the Internal Revenue Service began an examination of the corporation's tax years 1979 - 1985, and those of the LaRosa brothers, for 1981-1983. The IRS disallowed the completed contract method and, therefore, determined that the corporation had understated its income for the early years and overstated it for the later years. As a result, the Service shifted corporate income from the later to the earlier years, and attributed the income shifts to the brothers' returns. That income shift to the earlier years resulted in more taxes owed for those years (1981-1983), but overpayments in later years (1984-1985).

6. On December 3, 1985, the IRS made jeopardy assessments totaling more than $20 million, pursuant to IRC §6861, against the corporation, Joseph and Petitioners. Eventually, these assessments were reduced to $9.744 million (including tax of $3.4 million) after a settlement in the United States Tax Court.

7. Of the total, the jeopardy assessments against Petitioners totaled $6.3 million in tax, penalty and interest for 1981-1983.

8. To collect these assessments, the IRS simultaneously levied on property belonging to the LaRosas and the corporation. It was undisputed below that the total seized by the December 3, 1985 levies was at least $12 million in cash and cash equivalents, more than enough to pay all of the LaRosas' eventual tax bills, including the bills of Petitioners herein.

9. Despite these seizures, the government did not immediately apply the money to pay the taxes, as it normally does. However, it did apply one seizure of $282,669.00. Instead, 44 days later on January 16, 1986, the IRS entered into an "escrow" agreement with the LaRosa brothers and the corporation. Among other things, the escrow agreement, by its terms and in practice, provided that the cash was not to be used to pay the taxes, and that the LaRosas could not use the principal, but could use some of the income, subject to the IRS' approval. In fact, the principal was returned to the LaRosas on or about May 14, 1991 (after settlement in the Tax Court was concluded).

10. Shortly after the jeopardy assessments and seizures, the IRS issued statutory notices of deficiency to the Petitioners (as well as to the corporation and Joseph), as required by IRC §6212(a). Petitioners timely petitioned to

the United States Tax Court. The escrow was open during the five years that the Tax Court case was pending.

11. In May, 1991, all parties settled the Tax Court litigation for the lower figures described above. The IRS calculated interest on the tax as settled in the Tax Court, and the taxes, penalties and interest were fully paid at that time.

12. As noted, the IRS had refused to stop the running of interest on the Petitioners' tax deficiencies while the Tax Court litigation was pending (1986 through April 30, 1991), even though it held virtually all of their liquid assets in escrow. As a result, the Petitioners filed a claim for refund of that interest on April 23, 1993. Among other things, the claim argued that the IRS should have stopped the running of interest as of December 3, 1985, the date of the levies, because the Service had actual or constructive possession of their cash on and as of that date.

13. In March, 1994, the IRS refunded to the Petitioners approximately $1.5 million in interest, but did so on a basis different from the legal theory stated in the claim for refund. In December, 1995, the IRS formally denied the claim for refund despite having granted the refund at issue.

ESTOPPEL ISSUE

14. The $1.5 million refund was prompted, at least in part, by an inquiry made on behalf of the Petitioners through Congresswoman Constance Morella, who wrote to the Service requesting a review of the case. App. infra, Item 5. As a result, the case was given personal attention within the Internal Revenue Service. Immediately preceding the refund was a letter written by Joseph H. Cloonan, District Director of Internal Revenue*, to Congresswoman Morella dated March 24, 1994. (App. Item 5, infra.) In part, that letter stated that the IRS had eliminated the interest charged on the Petitioners' individual accounts for 1981 and 1982, and that Mr. LaRosa would receive refund checks for those years (though not for 1983). The letter goes on to state, "We are sorry that Mr. LaRosa's dealing with the Internal Revenue Service have been less than satisfactory. Please be assured that we share your concern

*The District Director is the highest IRS official in each IRS District and is responsible for general administration of the District, including oversight of branch chiefs. Internal Revenue Manual Section 11(12)1.1, 11(12)1.51. The District Director has authority to grant tax refunds. Treas. Reg. Section 601.103(b)(3).

that all taxpayers receive efficient and courteous treatment in their dealings with the Internal Revenue Service and that quality service is our ultimate goal. Please extend our apology to Mr. LaRosa for any inconvenience this may have caused."

15. Two years elapsed. In March, 1996, less than one month before its statute of limitations would have expired (IRC §6532(b)), the IRS sued the Petitioners to recover the $1.5 million, plus interest, as an "erroneous refund." IRC §7405. Petitioners' amended answer and counterclaim (App. infra, Item 6) alleged the defense of estoppel.

16. The estoppel and other issues were presented to the District Court on cross motions for summary judgment (supported by affidavits). The District Court held in favor of the government on all points.

17. With respect to the estoppel issue, the District Court ruled, 993 F. Supp at 916, that as a matter of law the government could not be estopped from suing under IRC §7405, adopting the following language from Miller v. United States, 949 F.2d 708, 712-713 (4th Cir. 1991):

> "Under relevant case law, it is clear that neither the government, nor a government agency such as the IRS, can be equitably estopped from asserting its legal rights because of the actions of an agent ... Furthermore courts expressly have prohibited the application of the doctrine of equitable estoppel in cases involving the IRS."

The District Court assumed the presence of the elements of estoppel (" ... it is hard to conjure a case where prior to such suit [a suit for erroneous refund] a taxpayer would not believe that the IRS had acted correctly and would not make use of the refund," 993 F.Supp. At 916) which elements were in any event well-pleaded and supported by evidence. It nevertheless ruled that "[t]he IRS is permitted to seek to undo such mistakes regardless of who is to blame for the error. There is nothing special about the case at bar in this regard." Id.

18. The Court of Appeals adopted this reasoning, effectively ruling in its Per Curiam opinion that equitable estoppel is unavailable as a matter of law, no matter what the circumstances of the case.

INTEREST ISSUE

19. In their counterclaim (App. *infra*, Item 6), the Petitioners argued that they were due a refund of interest paid because the IRS refused to stop the running of interest even though it had enough money on December 3, 1985, to full-pay the Petitioners' eventual liabilities.

20. While acknowledging that "Defendants are correct that the general rule requires the IRS to liquidate assets after a levy, and that the general effect of its failure to do so is to stop interest from running," 993 F. Supp. at 916, the District Court nevertheless held that the Defendants were not entitled to judgment on their counterclaim. It so concluded because of the presence of the escrow agreement which, according to the District Court, was a permissible option for the IRS under the levy statute, IRC §6335, and which allowed the IRS to continue to accrue interest on the Petitioners' tax liability despite the IRS having enough to pay it. On appeal, the Court of Appeals adopted this holding by silence.

REASONS FOR GRANTING THE PETITION

ESTOPPEL ISSUE

1. The Fourth Circuit's decision on the estoppel issue conflicts with the decisions of at least five other Circuits, both in principle and in the particulars of the case. Indeed, so striking is the disarray among the Circuits on the availability and extent of the doctrine estoppel as applied to tax cases that at least three distinct rules are discernable among them. This is aside from the rule in the Fourth Circuit, which is that the IRS can never be estopped by its actions, no matter how egregious.

2. The rule in the Ninth Circuit stems from Schuster v. Commissioner, 312 F.2d 311 (9th Cir. 1962). There, a bank distributed the corpus of a trust after having been informed that the trust was not included in the decedent's gross estate. Therefore, the bank no longer retained the property that was the subject of a tax deficiency and would have had to pay the tax out of its own funds. The Ninth Circuit believed this was enough to merit estoppel. While estoppel "should be applied against the government with utmost caution and restraint, . . . " Id., at 313, and while in general estoppel is not applicable to prevent the Commissioner from correcting an error (of law),

there are cases where someone might sustain "such a profound and unconscionable injury" as to require, "with any sense of justice and fair play, that the Commissioner not be allowed to inflict the injury." Id., at 317.

3. The rule in the Second Circuit is stated in Miller v. United States, 500 F.2d 1007 (2nd Cir. 1974), an action for tax refund in which a suit was brought after the jurisdictional deadline, but within an altered jurisdictional deadline set by the IRS's inadvertent mailing of a notice of claim disallowance. The Court held that estoppel applied. While the government generally cannot be estopped by the unauthorized act of its agents, here the act was authorized, even if it was erroneous.

4. The rule in the Eleventh Circuit appears to require the "traditional elements" of estoppel, plus "extreme circumstances." Feldman v. Commissioner, 20 F.3d 1128, 1134 (11th Cir. 1994). In an example of judicial understatement, that Court wrote, in part: "It is unclear precisely when the government may be equitably estopped." Id., at 1134.

5. Yet a different rule is illustrated by cases such as United States v. Guy, 978 F.2d 934 (6th Cir. 1992). There, the taxpayer alleged that his attorney had called the

IRS and written a letter to determine whether the IRS intended to take certain collection action. Claiming assurances that the IRS would refrain from collecting, the taxpayer changed his financial position in a domestic dispute with his wife. When the IRS then sought to collect, the taxpayer claimed estoppel. In the Sixth Circuit, the Court said, there must be "some affirmative misconduct" by a government agent as the basis for estoppel. Id., at 937. The Seventh Circuit had agreed with this standard. Kennedy v. United States, 965 F.2d 413 (7th Cir. 1992). And, in Henry v. United States, 870 F.2d 634 (Fed. Cir. 1989), the Federal Circuit opined that relief might be available where the absence of equitable relief would be "unconscionable." Id., at 636.

6. Even this Court has spoken with more than one voice on this issue. In Office of Personnel Management v. Richmond, 496 U.S. 414 (1990) ("OPM"), reh. denied Aug. 13, 1990, this Court reviewed the history of estoppel decisions in this Court, noting "the present confusion in this area of the law," Id., at 423 and acknowledging that "[t]he language in our decisions has spawned numerous claims for equitable estoppel in the lower courts." Id., at 422.

Moreover, in OPM this Court refused the invitation of the parties to craft a clarifying rule because the case was disposable on a "narrower ground of decision." Id., at 423. Included was this Court's refusal to announce a flat rule, requested by the Government, that the Government could never be estopped by the actions or statements of its agents under any circumstances.

7. The time has come to clarify the law.

8. In the case at bar, a very large refund was granted after painstaking investigation and careful thought, accompanied by an apology signed by the highest IRS official in the District, one clearly possessing the authority to make the refund. This is not the case of a low-level agent off on some unauthorized tangent. Had this case arisen in some other circuits, there would have been a triable issue, but not in the Fourth Circuit.

9. The issue concerns an important question of federal law, and is of great administrative importance because millions of refunds are granted each year.* No

*In 1996, over 88 million refunds of all types were issued. IRS Pub. IRS Pub. 55B (Data Book) (7-97), p.8.

taxpayer, let alone these Petitioners under the circumstances of this case, should have to wait two years until the erroneous refund statute of limitations expires before spending the refund to which the taxpayer assuredly believes he is entitled, for fear of a suit for erroneous refund. But the rule the Fourth Circuit has stated here would require just that. If the Fourth Circuit's denial of estoppel under the compelling facts at bar is allowed to stand, even the garden variety tax refund is under a cloud. The question presented will arise each and every time a taxpayer obtains a refund, and, by the Fourth Circuit's logic, would spend it at his peril.

10. Given the millions of tax refunds issued each year, at risk under the Fourth Circuit's rule, a national rule is needed to give assurance that citizens will be able to cash their tax refunds in justifiable reliance on the IRS in issuing it, without fear of a later government suit to reclaim that same refund.

INTEREST ISSUE

11. The Fourth Circuit's holding that the IRS has no duty to stop interest by crediting seized funds to a

tax debt contravenes a long line of cases in this Court, the holding of the Eighth Circuit on the same issue, and an array of statutory authority interpreted in these cases.

12. When the Internal Revenue Services seizes a taxpayer's money, it has a clear statutory duty. That duty is to pay the assessed tax. IRC §6342(a), entitled "Application of Proceeds of Levy", provides in pertinent part that "any money realized" by levy "shall" be applied in a certain order: the expenses of levy, the tax inherent in this property seizure, and the tax liability of the delinquent taxpayer. Similarly, Code Section 7406 provides:

> "All judgments and moneys recovered and received for taxes, costs, forfeitures and penalties shall be paid to the Secretary as collections of Internal Revenue taxes." [emphasis added]

And, IRC §7809(a) provides for the application of tax collections on a daily basis.

When such payment occurs, interest on the tax stops. IRC §6601(a).

13. These statutes respond to the long-standing principle that the "prompt and certain availability" of the revenue is an "imperious need" of the government. Bull v.

United States, 295 U.S. 247 (1935). Indeed, the laws which describe the IRS's duty when it receives money are part and parcel of a larger statutory plan under which the IRS may immediately obtain the money by jeopardy assessments, as happened here. See IRC §§ 6331, 6861.

14. In case after case, this Court has reinforced the government's immediate right to these moneys in the face of taxpayer challenges of various sorts. For example, in United States v. National Bank of Commerce, this Court reiterated the long-standing rule, holding:

> "This notice [the levy] gives the IRS the right to all property levied upon . . . , and creates a custodial relationship between the person holding the property and the IRS so that the property comes into the constructive possession of the government." Phelps v. United States, 421 U.S. 330, 334 (1975).

15. The decision of the Fourth Circuit is in conflict with this well-established line of authority. It is in further conflict with the same principle enunciated in a number of appellate decisions. Illustrative of these is United States v. Ruff, 99 F.3d 1559 (11th Cir. 1996), where the court stated that the levy power is designed to "enable the

government promptly to secure its revenues while competing claims are resolved." Id. at 1563, quoting United States v. National Bank of Commerce, supra*.

16. So much of the Fourth Circuit's reasoning was not truly in dispute; even the government acknowledged on brief that "under normal circumstances" the levies would indeed have operated to stop the running of interest (which would have resulted in the sustaining of Petitioners' counterclaim). But, said the government, this case is different because of the escrow. The District Court and, by adoption, the Court of Appeals, agreed.

17. The District Court held that Code Section 6335, entitled "Sale of Seized Property", somehow also applied to the cash seizure at issue here. In fact, the levy statutes nowhere mention the availability to anyone of an "escrow" as a post-levy remedy. The law is quite clear that

*The Fourth Circuit's decision conflicts in principle even with that Court's own prior rulings. See United States v. Eiland, 223 F.2d 118 (4th Cir. 1955), and United States v. Barlows, Inc., 767 F.2d 1100 (4th Cir. 1985), where the rule applying the value of levied property to taxes as of the date of seizure was extended to apply to certain non-cash property.

the IRS must either apply the cash to taxes or release the levy. Here, the IRS failed to do any of the things the law allowed and required, but entered into an escrow nowhere authorized by statute.

18. In upholding the District Court's ruling, the Fourth Circuit's decision conflicts not only with the Supreme Court and appellate decisions cited above, but also with the decision in St. Louis Union Trust Company v. United States, 617 F.2d 1293 (8th Cir. 1980) supplemented by Stone v. Commissioner, 47 TCM 1502 (1984) and Stone v. Commissioner, Memorandum Sur Order (U.S. Tax Court March 30, 1987) (App. infra, Item 7). In these related cases, the same issue as in the case at bar was presented, but a different rule was held to be the law.

19. In St. Louis Union Trust Co., Andrew Stone agreed with the Civil Division of the IRS to an escrow of funds pending the outcome of a civil action against him by the government. The IRS jeopardy assessed and levied the escrow. On appeal was the issue of whether the IRS could demand the escrow for taxes. The Court of Appeals held that it could. In supplemental proceedings in the Tax Court, it was further held that interest on the tax deficiency stopped as of the levy dates, because on those dates, the

IRS came into constructive possession of the escrowed funds. This was so regardless of the existance of the escrow and regardless of the lack of actual possession. The Tax Court quoted from United States v. National Bank of Commerce, supra, to support its holding:

> "... when respondent [IRS] levied on the income account in 1972, it had the right to demand immediate surrender of the funds... There were no legal actions pending at the time of the 1972 levy to delay respondant's seizure of the funds."

Stone, Mem. Sur Order, supra., at 5.

20. In St. Louis Union Trust Co. (and its supplemental lower court cases), the rule is therefore that an IRS levy is effective to seize the taxpayer's assets even if they are in escrow, and therefore operates to stop the running of interest at that point. In the instant case, the Fourth Circuit held to the contrary: the IRS was not required to stop the running of interest because the Petitioners' levied funds were being held in escrow. These cases are in conflict, and a uniform rule is necessary to assure the public that the IRS' seizures will at least be

applied right away to taxes, so as to stop the running of interest.

21. The right of taxpayers to have their taxes paid promptly by IRS seizures, and to not have their funds sitting in some escrow arrangement not sanctioned by any statute, is of great importance. The IRS issues over 3 million levies per year.* In giving the IRS the draconian power of the levy, Congress also attached some limits on what the IRS could do with this power: either pay the tax with the money (as is clearly intended by this power), or release the levy. If the Internal Revenue Service were permitted to enter into escrow agreements as to cash seizures (and thereby extend the time during which interest accrues), rather than either returning the money (by releasing the levy) or applying the money to taxes, taxpayers would be at a disadvantage and the Internal Revenue Service would be saddled with a tremendous administrative burden with endless negotatiations over terms and conditions. As Congress has seen fit to grant the power of immediate seizure to the Internal Revenue

*Pub. 55B, IRS Data Book (1996) at p. 23, Table 20.

Service, in fairness there should be a corresponding requirement to apply the money to taxes immediately, so as to stop the running of interest.

CONCLUSION

For the foregoing reasons, the petition for a writ certiorari should be granted.

Respectfully submitted,

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Dominick LaRosa and Catherine LaRosa

APPENDIX

1. Denial of Petition for Rehearing - Fourth Circuit
2. Per Curiam Decision - Fourth Circuit
3. Opinion and Judgment - District Court
4. Pertinent Statutes
5. Letters of Congresswoman Constance Morella and District Director Cloonan
6. Petitioners' Amended Answer and Countertclaim
7. Stone v. Commissioner, Mem. Sur Order

APPENDIX - Item 1

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

FILED
September 8, 1998

No. 97-2782
CA-96-980-DKC

UNITED STATES OF AMERICA
Plaintiff - Appellee

v.

DOMINICK LAROSA; CATHERINE LAROSA
Defendants - Appellants

On Petition for Rehearing with
Suggestion for Rehearing In Banc

The appellants' petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of this Court or the panel requested a poll on the suggest for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

For the Court,
/s/ Patricia S. Connor

CLERK

APPENDIX - Item 2

UNPUBLISHED

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v.

No. 97-2782

DOMINICK LAROSA; CATHERINE LAROSA,
Defendants-Appellants.

Appeal from the United States District Court
for the District of Maryland, at Greenbelt.
Deborah K. Chasanow, District Judge.
(CA-96-980-DKC)

Argued: June 4, 1998

Decided: July 10, 1998

Before WILKINSON, Chief Judge, MURNAGHAN, Circuit Judge, and SMITH, United States District Judge for the Eastern District of Virginia, sitting by designation.

Affirmed by unpublished per curiam opinion.

COUNSEL

ARGUED: Robert Gerald Nath, ODIN, FELDMAN & PITTLEMAN, P.C., Fairfax, Virginia, for Appellants. Annette Marie Wietecha, Tax Division, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Appellee. **ON BRIEF**: Loretta C. Argrett, Assistant Attorney General, Lynne A. Battaglia, United States Attorney, Richard Farber, Tax Division, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Appellee.

Unpublished opinions are not binding precedent in this circuit. See Local Rule 36(c).

OPINION

PER CURIAM:

This case arises out of a May 1, 1991 settlement between the Internal Revenue Service, Dominick LaRosa, and other taxpayers not relevant to this appeal. The taxpayers in that settlement had underpaid their taxes for the years 1981, 1982, and 1983 but had overpaid their taxes for the years 1984 and 1985. The parties agreed that the underpayments plus penalties and interest totaled approximately $9.7 million while the overpayments plus interest totaled approximately $6.1 million. In settlement of these claims, the Internal Revenue Service received a check for approximately $3.6 million. Subsequently, the IRS, believing it should not have charged interest on the entire amount of the underpayments after the overpayments had occurred, issued refunds totaling approximately $1.5 million. However, it later concluded that these refunds should never have been issued, and the United States filed

this suit against Dominick and his wife Catherine to recover the $1.5 million. *See* 26 U.S.C. §7405 (authorizing the government to bring a civil action to recover an erroneous refund). The LaRosas counterclaimed, challenging the interest assessed on various fraud penalties and arguing that interest should not have been charged after certain property was seized pursuant to a jeopardy assessment.

The district court granted summary judgment to the United States on both its claim and the LaRosas' counterclaims. With respect to the government's claim, the district court reasoned that the LaRosas were not entitled to the $1.5 million. This was true whether the 1991 settlement was viewed as refunding the LaRosas for the 1984-85 overpayments or as crediting those overpayments against the 1981-83 underpayments. If the transaction were treated as a refund, then the LaRosas continued to owe interest on the entire amount of the underpayments until May 1991 and were not entitled to the $1.5 million. If the transaction were treated as a credit, then the LaRosas were not entitled to any interest on the overpayments, since they would be immediately applied to the underpayments. With respect to the counterclaims, the district court reasoned that the particular jeopardy assessment did not stop the accrual of interest on the underpayments and that it lacked jurisdiction to consider the LaRosas' challenge to the interest on the fraud penalties.

Our review of the record, written, and oral submissions of the parties, and the appropriate legal standards persuades us of the correctness of the district court's grant of summary judgment to the United States. We therefore affirm that judgment on the reasoning set

forth in the district court's memorandum opinion, *United States v. LaRosa*, 993 F. Supp. 907 (D. Md. 1997).

AFFIRMED.

N:\DATA\CLIENT\35433\00001\MRCDO001

APPENDIX - Item 3

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF MARYLAND

UNITED STATES OF AMERICA	:
	:
	:
v.	:Civil Action
	:No. DKC 96-980
	:
DOMINICK LAROSA and	:
CATHERINE LAROSA	:

MEMORANDUM OPINION

This is an action brought by the United States of America ("Government") to recover refunds of interest on tax underpayments which it claims the Internal Revenue Service ("IRS") erroneously issued to defendants Dominick LaRosa and Catherine LaRosa ("Defendants") for the years 1981 and 1982. In turn, Defendants have filed a counterclaim seeking a larger refund than the IRS granted. Both parties have moved for summary judgment on all claims. No hearing is deemed necessary and the court now rules pursuant to Local Rule 105.6.

I. Standard of Review.

It is well established that a motion for summary judgment will be granted only if there exists no genuine

issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c); Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 250 (1986); Celotex Corp. V. Catrett, 477 U.S. 317, 322 (1986). In other words, if there clearly exist factual issues "that properly can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party," then summary judgment is inappropriate. Anderson, 477 U.S. at 250; see also Pulliam Inv. Co. v. Cameo Properties, 810 F. 2d 1282, 1286 (4th Cir. 1987); Morrison v. Nissan Motor Co., 601 F.2d 139, 141 (4th Cir. 1979); Stevens v. Howard D. Johnson Co., 181 F.2d 390, 394 (4th Cir. 1950). The moving party bears the burden of showing that there is no genuine issue as to any material fact. Fed. R. Civ. P. 56(c); Pulliam Inv. Co., 810 F.2d at 128 (citing Charbonnages de France v. Smith, 597 F.2d 406, 414 (4th Cir. 1979)).

When ruling on a motion for summary judgment, the court must construe the facts alleged in the light most favorable to the party opposing the motion. United States v. Diebold, Inc., 369 U.S. 654, 655 (1962); Gill v. Rollins Protective Servs. Co., 773 F.2d 592, 595 (4th Cir. 1985). A party who bears the burden of proof on a particular claim

must factually support each element of his or her claim. "[A] complete failure of proof concerning an essential element . . . necessarily renders all other facts immaterial." Celotex Corp., 477 U.S. at 323. Thus, on those issues on which the nonmoving party will have the burden of proof, it is his or her responsibility to confront the motion for summary judgment with an affidavit or other similar evidence. Anderson, 477 U.S. at 256.

In Celotex Corp., the Supreme Court stated:

> In cases like the instant one, where the nonmoving party will bear the burden of proof at trial on a dispositive issue, a summary judgment motion may properly be made in reliance solely on the "pleadings, depositions, answers to interrogatories, and admissions on file." Such a motion, whether or not accompanied by affidavits, will be "made and supported as provided in this rule," and Rule 56(e) therefore requires the nonmoving party to go beyond the pleadings and by her own affidavits, or by the "depositions, answers to interrogatories, and admissions on file," designate "specific facts showing that there is a genuine issue for trial."

Celotex Corp., 477 U.S. at 324. However, "a mere scintilla of evidence is not enough to create a fact issue." Barwick v. Celotex Corp., 736 F.2d 946, 958-59 (4th Cir. 1984) (quoting Seago v. North Carolina Theaters, Inc., 42 F.R.D.

627, 632 (E.D.N.C. 1966), aff'd, 388 F.2d 987 (4th Cir. 1967)). There must be "sufficient evidence favoring the nonmoving party for a jury to return a verdict for that party. If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted." Anderson, 477 U.S. at 249-50 (citation omitted).

II. Factual Background

This proceeding is only the later wrangling in a conflict which first erupted between the IRS and the LaRosas in the mid-1980's. These matters have involved the IRS, Defendants, Dominick LaRosa's brother, Joseph LaRosa, his father, Pietro LaRosa, and the family business, The LaRosa's International Fuel Co., Inc. (collectively "The LaRosas.") This is the second time that issues in this case have come before the federal courts in this Circuit, and prior proceedings have also been held before the United States Tax Court on more than one occasion. The parties have also apparently invested a great deal of time in negotiations. After Maryland state officials began to scrutinize the LaRosa's business activities in the mid-1980's, the IRS instituted its own investigation. Dominick LaRosa, Joseph LaRosa, and the LaRosa's International Fuel Co., Inc. were convicted on December 2, 1985 of tax

evasion in Maryland state court -- convictions for which they were pardoned by Governor William Donald Schaefer in 1992.[1/]

The IRS made a jeopardy assessment and levied on the LaRosas' assets on December 3, 1985 and the parties subsequently entered into an escrow agreement on January 16, 1986. Pursuant to the agreement, the LaRosas' assets were placed in escrow pending a determination of their federal tax liability. The escrow agreement prevented the IRS from liquidating the assets and stipulated that the assets were not taken as payment of any federal tax. While the assets were in escrow, the IRS controlled the funds, and the LaRosas needed approval for their household, legal, and other expenses.

In 1991, the parties reached a settlement which the United States Tax Court approved. See LaRosa v. Commissioner of Internal Revenue, Docket No. 6171-86. The parties agreed that the LaRosas had underpaid their

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It is odd that Defendants reacted with such outrage at the Government's mention of the LaRosas' state court convictions in regard to the initial assessment. The LaRosas had referred to the convictions in their IRS refund request, which they entered into the record as an exhibit to their Answer and Counterclaim.

taxes for the years 1981, 1982, and 1983 and that they had overpaid their taxes for the years 1984 and 1985. For purposes of the settlement, the parties agreed that the underpayments plus interest and penalties totaled $9,744,587 and that the overpayments plus interest and penalties totaled $6,120,204.[2/] By check, the LaRosas paid the Government the difference of $3,624,583.

The terms of the settlement specifically allowed the LaRosas to litigate in federal court the issue of interest assessed by the IRS. Subsequently, the LaRosas applied to the IRS for a refund claiming that interest should not have accrued after December 3, 1985, the date of the jeopardy assessment. That request was denied initially. In 1994, however, after intervention by the LaRosas' congressional representative, the IRS issued an apologetic letter and a refund. According to the parties, the IRS reasoned that the underpayments had been rectified as of the date of the receipt of the overpayments, and therefore interest on the underpayments should have ceased as of the dates of the

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2/ The overpayments arose because income which the LaRosas had claimed on the returns for the later years was transferred back to the prior years. The result was an overpayment for the years 1984 and 1985.

overpayments. The IRS abated $271,800 of 1981 interest and found that $239,651 of interest had accrued on that amount. The IRS also abated $827,658 of 1982 interest and found that $191,776 in interest had accrued on that amount. The IRS issued Defendants refunds which totaled $1,477,324.22 and a credit to their 1986 tax year of $53,561.28 resulting in a total refund of $1,530,085.50. Thus, although the LaRosas' original request for a refund was denied, the IRS used an alternative method to declare a refund. It is this refund which is presently at issue.

III. The Parties' Respective Positions

A. The Government's Claim

The Government claims that §7405(b) entitles it to a return of the $1,530,085.50 plus interest as an erroneous refund. See 26 U.S.C. §7405(b) 1994. Through its various filings, the Government has asserted a three-pronged argument.

First, the Government asserts that the refund was erroneous because the original calculations were correctly made under the provisions of §6601(a) of the Internal Revenue Code ("IRC") which provides for the accrual of interest on past due tax liabilities until those liabilities are paid. See 26 U.S.C. §6601(a) (1994). The Government

argues that rather than crediting the LaRosas' overpayments against the prior underpayments, it issued a refund of the overpayments in the form of the transfer on May 1, 1991. In other words, what appears as a credit merely was a refund which saved the stop of the Government handing a check to the LaRosas only to have the LaRosas hand a larger check back to the Government. As the argument goes, if the money was refunded then the overpayments never directly satisfied the underpayments and interest continued to run until the refund and check satisfied the liability on May 1, 1991. The Government points to a notation in Dominick LaRosa's brother Joseph LaRosa's records that the overpayment amounts constituted a "refund." The declaration of the IRS's Bedell Terry, Assistant Chief in charge of the Collections Division in Baltimore at the time, states that he gave the LaRosas the option of receiving the overpayment amount as a refund but not as a credit. Additionally, the Government argues that the allowance of interest, which it asserts would not have been allowable on a credit pursuant to IRS §6611(b)(1), but would have been allowable on a refund pursuant to IRC §6611(b)(2), demonstrates that the overpayment was refunded. See 26 U.S.C. §6611(b) (1994).

For their part, Defendants contend that the IRS actions were consistent with the application of a credit rather than a refund of the overpayment, thus the provisions of the IRC §6601(f) applied to stop the running of interest. Defendants also note that the amounts of the overpayments were sufficient, without the addition of interest, to pay the entire balance of the underpayments as of the 1985 overpayment. Therefore, they argue that the question of interest on the overpayments "does not even apply."

Defendants' argument is summarized as follows. When it receives an overpayment, the IRS may exercise its discretion to "credit the amount of such overpayment, including any interest allowed thereon, against any liability in respect of an internal revenue tax." 26 U.S.C. §6402(a) (1994). The Commissioner thus has the option of making a credit or issuing a refund. See Northern States Power Co. v. United States, 73 F.3d 764, 767 (8th Cir. 1996) (holding that the "the IRS has discretion whether to credit an overpayment to that liability or not"), cert. denied, 117 S.Ct. 168 (1996); Pettibone Corp. v. United States, 34 F.3d 536, 538 (7th Cir. 1994) (statute "leaves to the Commissioner's discretion whether to apply overpayments to delinquencies or to refund them to the taxpayer").

Issuance of a credit by the Commissioner triggers the effects of §6601(f). See Northern Power Co., 73 F.3d at 768 ("[T]he IRS may credit an overpayment against an outstanding liability, and if it does, Section 6601(f)'s netting provision comes into play."). This section provides:

> If any portion of a tax is satisfied by credit of an overpayment, then no interest shall be imposed under this section on the portion of the tax so satisfied for any period during which, if the credit had not been made, interest would have been allowable with respect to such overpayment.

26 U.S.C. §6601(f) (1994). Therefore, Defendants argue that, as the IRS exercised its discretion to apply a credit, interest on the underpayments should have ceased to accrue as of the dates of the overpayments. This is apparently the rationale which the IRS used to determine that a refund was due.

As the second prong of its argument, the Government asserts that even if the overpayments are treated as having been credited ("netted") against the underpayments, the particularities of this case prevent the interest halting effects of §6601(f) from applying to the LaRosas' underpayments. The United States posits that the "interest allowable" language indicates that interest should not have been calculated because interest "had already been

allowed on the tax overpayments from the dates they arose to April 30, 1991." This interpretation of the "interest allowable" language leads to the argument that the accrual of interest on the overpayment operated to negate the effect of stopping the interest on underpayments. The interest was no longer merely "allowable," the Government posits, because the IRS had "allowed" it.

In response, Defendants have argued that the language of §6601(f) can be read to demonstrate that interest must have stopped running. The statute, they argue, means that determination of whether interest stopped depends on whether interest would have been due on the overpayment had no credit been made. As interest clearly would have been allowable if the overpayment had been refunded, they argue, then the interest allowable prong is satisfied.

Finally, the United States argues that cessation of interest on the underpayments pursuant to §6601(f) must be accompanied by a cessation of interest owed on the overpayments. For support, the Government points to §6611 which governs interest on overpayments. The relevant language is as follows:

(a) Rate - Interest shall be allowed and paid upon any overpayment in respect of any internal revenue tax.

(b) Period -- Such interest shall be allowed and paid as follows:

(1) Credits - In the case of a credit, from the date of the overpayment to the due date of the amount against which the credit is taken.

(2) Refunds - In the case of a refund, from the date of the overpayment to . . . the date of the refund check.

26 U.S.C. §6611 (1994). The Government thus argues that, for interest to be allowed on a credited overpayment, the underpayment against which the credit is taken must arise subsequent to the overpayment. Although it admits that it could not find judicial authority on point, the Government provides scholarly support for its contention.[3/] Defendants have argued that the language of §6611 simply does not apply to the situation where a credit is taken against a prior underpayment. Further, they note that the reasoning which

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The Government points to 14 Stand. Fed. Tax Rep. (CCH) ¶40,335.011 and M. SALTZMAN, IRS PRACTICE AND PROCEDURE, ¶6.03(1)(b) (2nd ed. 1996).

one of the scholarly sources uses -- that the Government does not have use of the money prior to the underpayment and thus owes no interest -- is not applicable to the situation at bar. Defendants argue that the Government did in fact have use of the money prior to the settlement. Defendants also contend that the overpayments are not involved in this suit due to the principle that each tax year stands alone. Additionally, Defendants argue that §6402(a) allows for the crediting of an overpayment and "interest allowed thereon." Thus, they argue that it is irrelevant whether the interest was allowable in that the IRS allowed the interest.

Finally, Defendants have also argued that the Government should be estopped from recovering the refund. They claim to have reasonably relied on the IRS' issuance of the refunds to their detriment.

B. Defendants' Counterclaim

Defendants have argued that not only are they entitled to keep the refund which the IRS issued, but they are also entitled to an additional refund for two separate reasons. First, Defendants argue that interest was improperly charged on fraud penalties assessed in conjunction with the settlement. Second, they argue that

the IRS improperly rejected the reasoning in Defendants' refund request that interest should have stopped running even earlier than the dates which the IRS used in granting the contested refund.

As for the fraud penalty interest, Defendants have argued that no interest should have accrued before the tax court's decision became final. For support they point to the IRC §6601 (e)(2) which prevents interest from accruing on a penalty before ten days have passed from notice and demand for payment. See 26 U.S.C. §6601(e)(2) (1994). As they claim that pursuant to IRC §6213(a), 26 U.S.C. §6213(a) (1994), the IRS could not assess the penalty before the tax court's decision became final, no interest should have accrued as the penalty was promptly paid. This issue was not before the IRS on the LaRosas' refund request. Rather than argue the merits, the Government asserts that the Government is immune from a claim for a larger refund within the context of an action brought under §7405(b).

Defendants also argue that they were due a larger refund because December 3, 1985 (the date of the jeopardy assessment) should have been the date on which interest stopped running. They begin by asserting this Court's

jurisdiction over the claim for refund. They note that the elements required to establish jurisdiction are: (a) full payment of the tax assessed; (b) timely filing of a refund claim; and (c) timely filing of the refund suit. They argue that the interest sought to be abated was fully paid, that the refund claim was filed within two years of the payment date, and that the counterclaim was filed within two years of the claim denial.

For their argument that interest should have stopped running on their liability as of the date of the levy, Defendants rely upon case law to assert that the issuance of a levy reduces the property involved to the constructive possession of the Government. Once the property is in the constructive possession of the Government, they argue, interest is tolled even if the Government does not act expeditiously to liquidate. Defendants point to the tax court's 1987 holding in Stone v. Commissioner of Internal Revenue, Memorandum Sur Order, Docket No. 5311-72 and Stone v. Commissioner, 47 T.C.M. (CCH) 1502 (1984). There, the IRS issued a levy against an escrow account which Stone had established under an agreement with the Department of Justice. In a decision which did not involve the taxpayer, the IRS chose not to seize the account

immediately. The court held that the IRS had constructive possession of the funds in the escrow account as of the date of the levies because they could have ordered the bank to turn over the assets. The taxpayer was not held liable for the IRS' decision not to liquidate the accounts, and interest was thus held to cease as of the date of the levy.

Similarly, Defendants point to United States v. Barlow's, Inc., 767 F.2d 1098 (4th Cir. 1985), where the court held that interest ceased to accrue because the IRS had failed to conduct a prompt sale of the taxpayer's property "as soon as practical." In Barlow's, the taxpayer and IRS had agreed on the liability owed and the taxpayer had asked the IRS to levy on a debt owed to it by a third-party. The IRS levied, but rather than collect the entire liability, and without the involvement of the taxpayer, it entered into a payment agreement with the third-party under which the third-party defaulted. The court reasoned that the IRS' failure to collect the debt canceled the taxpayer's obligation to pay interest.

Defendants contend that the January 1986 escrow agreement does not differentiate this case from other levy situations where interest has been tolled because of the Government's constructive possession. Their main

argument is that the IRS's concurrence in entering the escrow agreement was equivalent to other concurrences with the third-party in Barlow's or the bank in Stone. Alternatively, they assert that the escrow should be ignored as the LaRosas were coerced by IRS agents who were threatening to liquidate Defendants' assets. Assuming the validity of the escrow agreement, Defendants assert that it is irrelevant that a portion of the money was used to pay for the Larosas' living expenses as they had no access to the principal, and the principal was at all times sufficient to pay the tax liability. Additionally, they claim that it is relevant that the value of the assets against which the IRS levied far exceeded the eventual liability.

Alternatively, Defendants argue that the IRS's cash-bond deposit procedure also supports their claim. See Rev. Proc. 84-58, 1984-2 C.B. 501. Under the cash bond procedure, the taxpayer's deposit of a cash bond stops interest from running unless the taxpayer revokes the bond. Even if the taxpayer attempts to revoke the payment, the IRS can refuse to return the funds if doing so would jeopardize eventual payment. No title is transferred before the eventual determination of the taxpayer's liability.

In response, the Government asserts that the precedent which Defendants rely upon is distinguishable, that the escrow was not entered into by way of Government coercion, that aspects of the escrow agreement demonstrate that the Government did not have constructive possession, and that the escrow account was not a cash bond. As for Barlow's, the Government contends that the Fourth Circuit's decision was based upon the IRC's directive that a sale be held as soon as practicable. See 26 U.S.C. §6335 (1994). The Government notes that, unlike in Barlow's, the tax liability was disputed and the LaRosas were involved in the IRS's decision to a\refrain from liquidating. AS for Stone, the Government argues that the consensual nature of the escrow and the benefits which the LaRosas received from the escrow, including the eventual return of all of the assets, are relevant distinctions.

Finally, the Government disputes Defendants' contention that the escrow agreement was the equivalent of a cash bond. The Government points out that a cash-bond is considered a payment, whereas the escrow agreement allowed the LaRosas' access to the assets while a bond would not have, and that the money was returned to the LaRosas with interest as opposed to without interest as with

a cash bond. The Government asserts that the cash-bond policy results in the Government having use of the funds, while the escrow agreement specifically prevented the Government from liquidating and using the assets or proceeds. Therefore, the Government argues that the policy behind the cessation of interest with a cash bond is absent from the case at bar.

IV. Analysis

A. The Government's Claim

As outlined above, the Government has argued along three lines of reasoning that summary judgment should be entered in its favor. As each of the Government's grounds stand alone, this Court will enter summary judgment in accordance with the standard of review detailed above if no material fact is in dispute with regard to any of these three approaches and either party is entitled to judgment as a matter of law.

This discussion begins with the Government's final argument -- that the refunds were erroneous because the computations failed to correspondingly abate the overpayment interest. What transpired on May 1, 1991 with regard to the 1984 and 1985 overpayments was either a refund or a credit. If it was a refund, then the law is clear

-- the subsequent refund of interest paid on the 1981-1983 underpayments was erroneous as no payments for those tax years was received until May 1, 1991 and thus nothing operated to stop interest from accruing on either the underpayment or the overpayment. See 26 U.S.C. §6601(a) (1994); 26 U.S.C. 6611(b) (1994).

If, on the other hand, the May 1, 1991 transaction is construed as application of credit of the 1984 and 1985 overpayments against the earlier underpayments as of the dates of the overpayments, then interest should not have run on either the overpayments or the underpayments as of the applicable dates. In this situation as well, it would be error to abate interest only on the underpayments and not also on the overpayments. The Government would still be entitled to recover the erroneous refund.

The provisions of §6601(f) only apply when an overpayment is credited. 26 U.S.C. §6601(f) (1994). Defendants have not claimed otherwise. The interest tolling effects of §6601(f) create a type of legal fiction that payment was made on a certain prior date. That is what differentiates a credit from a refund, where the money would then need to be turned back over to the Government to satisfy any prior liability and the provisions of §6601(a)

would apply. This fiction is sensible, as it is illogical that the Government would owe any interest to a party which has paid an undisputed liability. Likewise, it would be illogical to charge a taxpayer interest after it had paid its liability. Money can only lie in one pocket. Therefore, it the tax is paid, the funds belong to the Government and the taxpayer has no claim to any interest. Therefore, presuming that netting occurred, the proper figures to use should not have included post-April 15, 1986 interest on either side of the equation. Defendants' argument that the Government had their money prior to the settlement is fallacious, as what the Government had was its own money, if the credit analysis is used. A proper reexamination of the settlement as a credit would have taken this into account. Thus, the Government is entitled to summary judgment on its claim for a recoupment of the refund unless one of the Defendants' remaining technical arguments bars that result.

Defendants have posited that reexamining the interest allowed on the overpayments was improper given the principle that each tax year stands alone. There is no doubt that this is an axiomatic principle of our tax system. See Heiner v. Mellon, 304 U.S. 271, 275 (1938); Commissioner v. Sunnen, 333 U.S. 591, 598 (19480);

United States v. Consolidated Edison, 366 U.S. 380, 384-85 (1961). However, as the cases which Defendants cite and the cases cited therein reveal, its applicability relates to the timing of the reporting of income and the taking of deductions. It is simply not the case that when an overpayment is credited against an underpayment, a reevaluation of the size of the underpayment does not require a reevaluation of the amount of the overpayment which constituted the credit. To say otherwise would be the equivalent of declaring a refund by only looking at the liability and not at the payment for the year in question. Years when overpayments are made and years when underpayments occur become linked differently than years when income is received which resulted from a business activity or contested liability in a prior year. It is in the latter cases, rather than the former, where the tax year must stand alone.[4/]

Defendants also argue that because the IRS allowed such interest, whether or not it was allowable, rectifying

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It is also hard to believe that, after all the emotional turmoil which Defendants claim to have suffered, they would encourage the Government to initiate a separate action to recover overpayment interest for 1984 and 1985.

this error would be improper. The language of §6402(a) does say that credits consist of "overpayment, including any interest allowed thereon." 26 U.S.C. §6402(a) (1994). However, when reexamining the question of interest within the framework of a credit, Defendants point to no authority (beside the annual accounting concept dismissed above) which estops the IRS from correcting the mistaken allowance of interest on a credit which clearly should not have been allowed under 6611(b)(1). The scholarly authority which the Government cited, and the IRS's administrative interpretations, which neither party cited, both support the contention that interest on overpayments used for credits is only allowed when the liability occurs subsequent to the overpayment.

In 1960, the IRS released Revenue Procedure 60-17, which dealt with the subject of restricted interest --or "provisions in law which limit or prohibit interest under certain conditions." Rev. Proc. 60-17, 1960-2 C.B. 942. In discussing §6611(b)(1), the Revenue Procedure clearly states that no interest is allowable on an overpayment which is credited against a liability for prior unpaid taxes. Id. As Defendants point out, the Supreme Court held in Helvering v. Winmill, 309 U.S. 79 (1938), that "[t]reasury

regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." Id. At 83. Thus, if the IRS netted the payments, it was not allowed to credit interest subsequent to the overpayment date. If treated as a credit when correcting the erroneous assessment of interest on the underpayments, the IRS should have correspondingly rectified this error.

The Revenue Procedure is also instructive in assuring that the IRS has no authority to grant restricted interest by consent. The Revenue Procedure notes that "[t]he payment of interest is mandatory on underpayments and overpayments of any internal revenue tax unless specifically prohibited by law or by mutual agreement." Rev. Proc. 60-17, 1960-2 C.B. 942. Nowhere does the document state the corollary which Defendants' argument would require -- that interest can be allowed by mutual consent when specifically prohibited. Therefore, no technicality bars the Government from seeking restitution of this erroneous refund. As the Government is entitled to summary judgment on the grounds specified above, it is unnecessary to reach the merits of its alternative arguments.

Defendants have also asserted that the Government should be estopped from seeking restitution. The Fourth Circuit's opinion in Miller v. United States, 949 F.2d 708 (4th Cir. 1991), is instructive in this regard. In that case, Miller was the executor of an estate which involved a holographic will. As the residuary clause of the will was vague, Miller filed an action in Virginia state court seeking a determination of the clause's validity. At the same time, he contacted the IRS to determine how much estate tax to pay. The attorney with whom he consulted stated that he should pay the entire amount as any excess would be refunded subsequent tot he probate court's finding. The IRS attorney did not advise Miller to file a refund claim and he did not do so until after the statutory period had run. The IRS denied the claim on the ground that it was untimely. The Fourth Circuit affirmed the district court's summary judgment ruling in favor of the IRS. With regard to equitable estoppel, the Fourth Circuit held:

> Under relevant case law, it is clear that neither the government, nor a government agency such as the IRS, can be equitably estopped from asserting its legal rights because of the actions of an agent... Furthermore, courts expressly have prohibited the application of the doctrine of equitable estoppel in cases involving the IRS.

Id. At 712-13 (citations omitted). The Fourth Circuit has also observed that "equity generally plays a very limited role in tax cases." Webb v. United States, 66 F.3d 691, 694 (4th Cir. 1995), cert. denied, 117 S. Ct. 1079 (1997). Furthermore, the statute could not be clearer that the IRS may seek the return of an erroneous refund. See 26 U.S.C. §7405(b) (1994). Barring certain knowledge that a refund was issued in error, it is hard to conjure a case where prior to such suit a taxpayer would not believe that the IRS had acted correctly and would not make use of the refund. While the IRS ought to strive to avoid issuing the type of erroneous refund which occurred in this case, the IRS is permitted to seek to undo such mistakes regardless of who is to blame for the error. There is nothing special about the case at bar in this regard. Therefore, the Government cannot be estopped from seeking its §7405(b) rights.

B. Defendants' Counterclaim

In the initial refund request and in their counterclaim, Defendants assert that the jeopardy assessment and levy on their property served to toll the running of interest on the underpayments. This argument

here can be restated as "I want my cake and to eat it too."[5/] Defendants are correct that the general rule requires the IRS to liquidate assets after a levy, and that the general effect of its failure to do so is to stop interest from running. See e.g., United States v. Barlow's, Inc., 767 F.2d 1098 (4th Cir. 1985) (discussed above); 26 U.S.C. §6335 (1994) (stating that the IRS must conduct a sale "as soon as practicable"). However, the statutory formulation of the IRS's duty as "as soon as practicable" allows this Court to sanction an agreement between the parties which makes liquidation prior to a final tax court decision not practicable. Practical delays can either result from the IRS's own needs or from what the IRS views as within the practical needs of itself and the taxpayer. Here the delay arose because the taxpayer sought it. Furthermore, nothing in the record suggests that Defendants were coerced. As they readily admit, the IRS had unambiguous statutory authority to

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This saying has been used, in various forms, so often that citation to its origin is unnecessary. It appears, however, to derive from George Herbert's 1633 work, The Size, where he wrote "Wouldst thou both eat they cake and have it?" See JOHN BARTLETT, FAMILIAR QUOTATIONS, 142 n. 16 (16th ed. 1992).

liquidate the LaRosas' assets. The LaRosas also availed themselves, unsuccessfully, of legal means to challenge the amount of the jeopardy assessment. See LaRosa v. United States, 841 F.2d 544 (4th Cir. 1988). That the LaRosas held little sway in the negotiations is purely a function of their disadvantageous legal position. Driving a hard bargain does not amount to coercion. Simply put, the IRS did the LaRosas a favor by entering into an escrow agreement which allowed the LaRosas to maintain their business operations. Additionally, the Government is correct in arguing that the relative size of the assessment to the adjudicated liability is irrelevant as the assessment was approved by the courts.

Additionally, Defendants' argument that the escrow agreement was, in essence, a cash bond is meritless. In order to gain the benefits of the cash bond system, the LaRosas should have followed the requirements involved. See Rev. Proc. 84-58, 1984-2 C.B. 501. They do not claim to have done so. Creating judicial regimes which parallel regulatory processes is dangerous and courts should avoid doing so. As no statute provides for treating an escrow agreement as a cash bond, such a regime would be the product of equity and, as discussed above, equity has sparse

applicability in the tax law context. As Justice Felix Frankfurter wisely counseled, "[O]ne should sail close to the shore of literalness in dealing with the technical problems which are the subject matter of revenue laws." See Lewyt Corp. V. Commissioner of Internal Revenue, 349 U.S. 237, 249 (1955) (Frankfurter, J. dissenting). The regulations allow for cash bonds and only cash bonds.

Therefore, by mutually consenting to enter into the escrow agreement, the parties relieved the IRS from its §6335 duty to liquidate and interest continued to run until the date of the overpayment credit or payment. In addition to being legally sound, this result makes the most sense from the standpoint of pragmatism. There are a number of possibilities following an IRS levy. First, the IRS can liquidate. As Defendants submit, such a liquidation would have disastrous side effects on the taxpayer should the assessment be erroneous. As an alternative, the cash bond rules provide an option for a taxpayer who wishes to contest a liability yet ensure itself that the opportunity costs would not include interest. To do so, however, the maker of a cash bond pays the price of losing access to the underlying asset and of never recouping the interest lost pending a final outcome. The escrow arrangement is a

solid middle ground for both parties. The IRS is assured that the liability would be paid and the taxpayer does not face the liquidation or complete freeze of its assets. The result for which Defendants' argue would undoubtedly dissuade the IRS from entering into escrow agreements following future jeopardy assessments. Therefore, the legally sound result also happens to generate the best outcome.

Summary judgment in favor of the United States also is appropriate with regard to interest on the fraud penalties. As the Fourth Circuit held, "[w]ith respect to suits against it for tax refunds, of course, the United States has to some extent waived its sovereign immunity." Webb v. United States, 66 F.3d 691, 693 (4th Cir. 1995). The same case notes that the statutory provisions allowing for jurisdiction over a refund claim mandate that the petitioner have filed a timely refund claim with the IRS. Id. Defendants recognize as much in their own filing where they note that the jurisdictional prerequisites for a refund claim include that the assessment was paid, that the refund claim was timely filed, and that the action before the federal court was also timely. Here, Defendants' refund claim failed to contest the interest which the IRS assessed

on the fraud penalties. In order to assert jurisdiction following a refund claim, the claim before the IRS must have specifically addressed any ground on which the District Court action is based. See Miller v. United States, 949 F.2d 708, 711 (4th Cir. 1991) (noting, within context of informal claim for refund, that a claim need be "sufficiently specific to apprise the IRS that the taxpayer desires a refund and to pin-point the area of dispute, thereby facilitating an examination of the claim if appropriate"). Therefore, this Court would not have original jurisdiction over this aspect of Defendants' counterclaim.

The only avenue for Defendants to assert jurisdiction is if the claim arises under the recoupment exception to Fed. R. Civ. P. 13(d). The recoupment exception allows that "when the United States institutes an action, defendant may assert by way of recoupment any claim arising out of the same transaction or occurrence as the original claim in order to reduce or defeat the Government's recovery." 6 C. Wright & A. Miller, Federal Practice and Procedure §1427 (1990). Thus, the issue presented here is whether the refund which the Government seeks to recover and a refund for interest incorrectly

charged on the fraud penalties arise out of the same transaction or occurrence.

In assessing this issue, the following factors must be examined: (I) whether issues of fact and law raised by the claim and counterclaim are largely the same; (ii) whether substantially the same evidence bears on both claims; and (iii) whether any logical relationship exists between the two claims. See Whigham v. Beneficial Finance Co., 599 F.2d 1322, 1323 (4th Cir. 1979). As for the first element, the questions of law which the claim and counterclaim raise are different. The basis of the refund was the abatement of interest on the underpayments. The interest granted on the overpayments was necessarily related as it formed the credit which satisfied the underpayments. The question of when interest would begin to run on a fraud penalty, however, is entirely distinct as it involves entirely different sections of the IRC. This difference is sufficient to overcome the relatively low level of evidentiary difficulty which adjudicating the claim would present and the tangential relationship which exists by virtue of the involvement of both issues within the context of the tax court settlement. Although these issues arise out of the same tax years, this relationship ends there. The

assessment of the penalty relates solely to the principal of the underpaid tax rather than any interest due thereon. See 26 U.S.C. §6653(b)(1) (1994) (stating that a fraud penalty is equal to "75 percent of the portion of the underpayment which is attributable to fraud"). Thus, the determination of interest due on the underpayments does not affect the size of the fraud payments. Therefore, Defendants may not assert such a claim under the recoupment exception.

V. Conclusion

For the foregoing reasons, summary judgment must be entered in favor of the United States both on the Government's claim for restitution of the erroneously granted refund and on Defendants' counterclaims. Defendants are liable to the Government in the amount of $1,530,085.50 plus interest under IRC §6602 "from the date of the payment of the refund." 26 U.S.C. §6602 (1994); see e.g., United States v. Mallah, 882 F. Supp. 779, 781 (S.D. Ind. 1995). Counsel are directed to prepare an appropriate order of judgment.

DEBORAH K. CHASANOW
United States District Judge

APPENDIX - Item 4

SEC. 6335 SALE OF SEIZED PROPERTY.

(b) NOTICE OF SALE. --The Secretary shall as soon as practicable after the seizure of the property give notice to the owner, in the manner prescribed in subsection (a), and shall cause a notification to be published in some newspaper published or generally circulated within the county wherein such seizure is made, or, if there be no newspaper published or generally circulated in such county, shall post such notice at the post office nearest the place where the seizure is made, and in not less than two other public places. Such notice shall specify the property to be sold, and the time, place, manner, and conditions of the sale thereof. Whenever levy is made without regard to the 10-day period provided in section 6331(a), public notice of sale of the property seized shall not be made within such 10-day period unless section 6336 (relating to sale of perishable goods) is applicable.

SEC. 6342. APPLICATION OF PROCEEDS OF LEVY.

(a) COLLECTION OF LIABILITY. --Any money realized by proceedings under this subchapter (whether by

seizure, by surrender under section 6332 (except pursuant to subsection (c)(2) thereof), or by sale of seized property) or by sale of property redeemed by the United States (if the interest of the United States in such property was a lien arising under the provisions of this title) shall be applied as follows:

(1) EXPENSE OF LEVY AND SALE. --First, against the expenses of the proceedings;

(2) SPECIFIC TAX LIABILITY ON SEIZED PROPERTY. --If the property seized and sold is subject to a tax imposed by an internal revenue law which has not been paid, the amount remaining after applying paragraph (1) shall then be applied against such tax liability (and, if such tax was not previously assessed, it shall then be assessed);

(3) LIABILITY OF DELINQUENT TAXPAYER. --The amount, if any, remaining after applying paragraphs (1) and (2) shall then be applied against the liability in respect of which the levy was made or the sale was conducted.

SEC. 6343. AUTHORITY TO RELEASE LEVY AND RETURN PROPERTY.

(a) RELEASE OF LEVY AND NOTICE OF RELEASE. --

(1) IN GENERAL. -- Under regulations prescribed by the Secretary, the Secretary shall release the levy upon all, or part of, the property rights to property levied upon and shall promptly notify the person upon whom such levy was made (if any) that such levy has been released if--

(A) the liability for which such levy was made is satisfied or becomes unenforceable by reason of lapse of time,

(B) release of such levy will facilitate the collection of such liability,

(C) the taxpayer has entered into an agreement under section 6159 to satisfy such liability by means of installment payments, unless such agreement provides otherwise,

(D) the Secretary has determined that such levy is creating an economic hardship due to the financial condition of the taxpayer, or

(E) the fair market value of the property exceeds such liability and release of the levy on a part of such property could be made without hindering the collection of such liability.

For purposes of subparagraph (C), the Secretary is not required to release such levy if such release would jeopardize the secured creditor status of the Secretary.

SEC. 7406. DISPOSITION OF JUDGMENTS AND MONEYS RECOVERED.

All judgments and moneys recovered or received for taxes, costs, forfeitures, and penalties shall be paid to the Secretary as collections of internal revenue taxes.

SEC. 7809(a). DEPOSIT OF COLLECTIONS.

(a) GENERAL RULE. -- Except as provided in subsections (b) and (c) and in sections 7651, 7652, 7654, and 7810, the gross amount of all taxes and revenues received under the provisions of this title, and collections of whatever nature received or collected by authority of any internal revenue law, shall be paid daily into the Treasury of the United States under instructions of the Secretary as internal revenue collections . . .

APPENDIX - Item 5

CONGRESS OF THE UNITED STATES
House of Representatives
March 28, 1994

Mr. Dominick LaRosa
10 Tobin Ct.
Potomac, MD 20854-4545

Dear Mr. LaRosa:

The enclosed letter from the Internal Revenue Service is a response to my inquiry on your behalf. I hope the information is helpful.

Thank you for providing me with this opportunity to be of assistance. If I can be of assistance on the Federal level in the future, please contact my district office again.

Sincerely,

Constance A. Morella
Member of Congress

CAM:kat
Enclosure

Internal Revenue Service

Department of Treasury

Director

Mid-Atlantic Region
P.O. Box 69, Bensalem, PA
19020

Internal Revenue
Service Center

Philadelphia, PA

The Honorable Constance A. Morella
Representative in Congress
51 Monroe Street, Suite 507
Rockville, MD 20850

Dear Representative Morella:

Thank you for your correspondence dated December 17, 1993, written on behalf of Mr. Dominick LaRosa, concerning interest charged for the years 1981, 1982 and 1983 on his individual and business accounts.

This is to confirm the telephone conversation between Ms. Janet Giuliani of your office and Ms. Elizabeth Lee, a member of my staff.

Our records show the additional tax and interest charged December 3, 1985 on the Form 1120, U.S. Corporation Income Tax Return, accounts for the years 1981, 1982 and 1983 have been eliminated.

Based on the information submitted, we have eliminated the interest charged on your constituent's individual accounts in the amount of $271,800.46 for the tax year 1981 and $827,658.25 for the year 1982. Mr. LaRosa will

receive refund checks for 1981 and 1982 in a few weeks if there are no other outstanding balances due.

Further review of the 1983 individual account shows that the additional tax of $955,321.00 was partially decreased in the amount of $487,240.00. When we recomputed the interest, it was determined that the interest originally charged on the additional tax was not correct. Therefore, the correct interest amount of $573,224.00 will remain.

We are sorry that Mr. LaRosa's dealing with the Internal Revenue Service have been less than satisfactory. Please be assured that we share your concern that all taxpayers receive efficient and courteous treatment in their dealings with the Internal Revenue Service and that quality service is our ultimate goal. Please extend our apology to Mr. LaRosa for any inconvenience this may have caused. We appreciate your interest in this matter. If there are any further questions, you may contact Ms. Elizabeth Lee at (215) 969-2164 (not toll free) Monday through Friday between the hours of 7:00 a.m. and 3:00 p.m.

Sincerely,

Joseph H. Cloonan
Director

Attachments

APPENDIX - Item 6

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND
Southern Division

UNITED STATES OF AMERICA	*
	*
Plaintiff,	*
	*
v.	*CIVIL ACTION
	NO. DKC 96-980
	*
DOMINICK LAROSA	*
and	*
CATHERINE LAROSA	*
	*

Defendants.

AMENDED ANSWER AND COUNTERCLAIM
OF THE DEFENDANTS
DOMINICK LAROSA AND CATHERINE LAROSA

The Defendants, Dominick LaRosa and Catherine LaRosa, for their amended answer and counterclaim, by undersigned counsel, respond as follows to the allegations of the Complaint.

AFFIRMATIVE DEFENSES

1. This action is barred by the applicable period of limitations.

2. The Plaintiff is estopped from claiming that erroneous refunds were issued to Defendants, as alleged in the Complaint, because, among other reasons, the Defendants reasonably relied to their detriment on the Plaintiff's issuance of the tax refunds to use the refunds for their business and personal purposes; Defendants did not know such refunds were erroneous but believed such refunds were correctly issued; the refunds were authorized and issued by Plaintiff's agents acting within the scope of their authority; and it would be unconscionable not to grant equitable relief to Defendants under the circumstances.

3. As a matter of fact and law, interest on the Defendants' tax liabilities for the tax years 1981, 1982 and 1983 ceased to accrue as of the dates the Plaintiff's agency, the Internal Revenue Service, levied upon or seized Defendants' assets pursuant to jeopardy assessments made on December 3, 1985, because Plaintiff had actual and/or constructive possession of Defendants' property as of the dates of such levies.

4. As a matter of fact and law, Plaintiff's method of administering and operating an escrow account into which Defendants' property was placed pending settlement of Defendants' tax liabilities for 1981-1983 gave

Plaintiff actual or constructive possession of such property, so that interest on Defendants' tax liabilities for 1981-1983 ceased as of the dates of the IRS' levies.

5. The Substantial Understatement Penalty (IRC §6661) was erroneously assessed against the Defendants for 1982 since the fraud penalty was also assessed for that year.

6. As a matter of fact and law, the Plaintiff is not entitled to interest on the fraud penalties it assessed against Defendants.

7. The Plaintiffs's method of calculating the refunds at issue in part correctly provided for interest on Defendants' overpayment for the tax year 1985 and, with exceptions, correctly credited the 1985 overpayment tot he underpayments for the tax years 1981 and 1982 as of April 15, 1986, or as of the earlier dates in the case of payments made prior to April 15, 1986; however the Plaintiff's method of calculating interest, as a matter of fact and law, should have resulted in larger refunds for 1981 and 1982, and should have resulted in a refund for 1983.

8. The amounts of the refunds issued to Defendants were erroneously understated, in that Plaintiff, as a matter of fact and law, was required to apply the value

of all of Defendants' levied and escrowed property, as of the dates of seizure of such cash and property, to the tax, penalty and interest that were determined with finality in April, 1991 as a result of the Decision of the United States Tax Court in Dominick LaRosa, et al., v. Commissioner of Internal Revenue, DKT No. 6171-86.

ADDITIONAL RESPONSE

In further response, the Defendants address the numbered allegations of the Complaint as follows:

1-6. Admitted.

7-24. The Defendants currently lack the knowledge or information sufficient to form a belief as to the truth of allegations in paragraphs 7-24, inclusive, except that as to paragraphs 10-18, the Defendants admit that the LaRosas entered into a stipulated decision in the United States Tax Court.

WHEREFORE, the Defendants respectfully pray:

a. That this Court adjudge and decree that the United States did not erroneously issue a refund to the Defendants, in any amount, relating to any tax year, including the tax years 1981-1986;

b. That this Court deny judgment to the United States in any amount for its alleged erroneous refund;

c. That this Court adjudge and decree the Defendants are not indebted to the United States in any amount, and that the Complaint be dismissed with prejudice;

d. That the Defendants be awarded their costs in this action and any further relief to which they may be entitled.

COUNTERCLAIM

COUNT I

25. This Counterclaim is for a refund of Federal taxes (including interest and/or penalties) paid by the Defendants to the Plaintiff, the United States of America.

26. Jurisdiction of this Counterclaim is authorized under Sections 1340 and 1346(a)(1), Title 28, United States Code, as this is a counterclaim for Federal taxes erroneously or illegally assessed or collected.

27. Venue lies in this Court pursuant to Section 1396 of Title 28, United States Code.

28. On or about December 3, 1985, the Defendant, through its agency, the Internal Revenue Service, made a jeopardy assessment of income taxes and additions thereto against the Defendants, Dominick and

Catherine LaRosa, with respect to the tax years 1981, 1982, and 1983.

29. Upon information and belief, subsequent to the assessments described above, the Defendants fully paid the taxes assessed against them.

30. Following the assessments and payments described above, the Defendants filed a claim for refund with the Internal Revenue Service, claiming that the amounts assessed against and paid by them were erroneous and that they were due a refund. Upon information and belief, a true and correct copy of this claim for refund is attached as Exhibit A.

31. Following this claim for refund, the Internal Revenue Service granted the claim for refund in part, and refunded to the Defendants certain funds in amounts to be determined.

32. More than six months have elapsed since the claim for refund described above was filed.

33. Upon information and belief, the Internal Revenue Service failed to refund to the Defendants the full amount to which they were entitled under their claim for refund for the years 1981, 1982 and 1983.

34. Upon information and belief, the Internal Revenue Service was required to credit, against the jeopardy assessments it had made, the full amount of any and all seizures it subsequently made pursuant to those jeopardy assessments, and to credit said amounts as of December 3, 1985.

35. As of December 3, 1985, the Internal Revenue Service had actual and/or constructive possession of Defendants' properties and was required by law to credit the full amounts and full value of those properties against the assessments it had made as of that date.

36. As a matter of fact and law, interest on the Defendants' tax liabilities for the tax years 1981, 1982, and 1983 ceased to accrue as of the dates the Plaintiff's agency, the Internal Revenue Service, levied upon or seized Defendants' assets pursuant to jeopardy assessments made on December 3, 1985, because Plaintiff had actual and/or constructive possession of Defendant's property as of the dates of such levies.

37. As a matter of fact and law, Plaintiff's method of administering and operating an escrow account into which Defendants' property was placed pending settlement of Defendants' tax liabilities for 1981-1983 gave

Plaintiff actual and/or constructive possession of such property, so that interest on Defendants' tax liabilities for 1981-1983 ceased as of the dates of the IRS' levies.

38. As a matter of fact and law, the Plaintiff is not entitled to interest on the fraud penalties it assessed against Defendants.

39. With exceptions, the Plaintiff's method of calculating the refunds at issue in part correctly provided for interest on Defendant's overpayment for the tax year 1985 and correctly credited the 1985 overpayment to the tax year 1981 and 1982 underpayments as of April 15, 1986, or earlier dates in the case of payments made prior to April 15, 1986; however, the Plaintiff's method of calculating interest, as a matter of fact and law, should have resulted in larger refunds for 1981 and 1982, and should have resulted in a refund for 1983.

40. The amounts of the refunds issued to Defendants were erroneously understated, in that Plaintiff, as a matter of fact and law, was required to apply the value of all of Defendants' levied and escrowed property, as of the dates of seizure of such cash and property, to the tax, penalty and interest that were determined with finality in April, 1991 as a result of the Decision of the United States

Tax Court in Dominick LaRosa, et al., v. Commissioner of Internal Revenue, DKT No. 6171-86.

41. Despite the methodology employed as described above, the Plaintiff failed to give Defendants credit (from their 1985 overpayment) for certain overpayments as of April 15, 1986.

COUNT II

42. Upon information and belief, in 1991 the Internal Revenue Service caused assessments against the Defendants as to the tax years 1981 and 1982 to be "paid" by the transfer, to those tax years, of positive credits from the Defendants' account with the Internal Revenue Service for 1985 or other years.

43. Upon information and belief, the "payments" (by transfer of credits) described above were made in 1991, by the Defendants.

44. Upon information and belief, the Internal Revenue Service, at some time in 1994, determined that the above-described credit transfer should have been effective as of April 15, 1986, or some date or dates earlier than in 1991.

45. Upon information and belief, based on the determination described above, the Internal Revenue

Service made the refunds to the Defendants that are at issue in the instant suit.

46. Upon information and belief, the refunds described above were not erroneous.

47. In the alternative, upon information and belief, the refunds described above should have been larger because the Internal Revenue Service should have transferred the credits effective as of an earlier date or dates, and should have refunded interest for the year 1983.

48. On these and other grounds, the refunds received by the Defendants were not erroneously issued, and the Defendants are entitled to additional payments of interest from the Internal Revenue Service for the tax years 1981, 1982 and 1983 in an amount to be determined by the Court.

WHEREFORE, the Defendants respectfully pray:

1. That this Court adjudge and decree that the Plaintiff, United States of America, is indebted to the Defendants, Dominick LaRosa and Catherine LaRosa, on the Counterclaim of the Defendants in an amount to be determined.

2. That this Court grant judgment in favor of the Defendants, and against the United States of America on the Counterclaim of the Defendants, in an amount to be determined by the Court.

3. That the Defendants be granted such other and further relief with respect to their Counterclaim as is merited under law.

Respectfully submitted,
DOMINICK LAROSA and
CATHERINE LAROSA,
Defendants
By Counsel

Robert G. Nath, Esq.
Odin, Feldman & Pittleman, P.C.
9302 Lee Highway, Suite 1100
Fairfax, Virginia 22031
(703)218-2121

CERTIFICATE OF SERVICE

It is hereby certified that copies of the foregoing Response, Amended Answer and Counterclaim were caused to be mailed by United States mail, postage prepaid, this 27th day of September, 1996, addressed as follows:

James J. Wilkinson, Esq.
Trial Attorney, Tax Division
U.S. Department of Justice
P.O. Box 227, Ben Franklin Station
Washington, DC 20044

_____

Robert G. Nath

N:\DATA\CLIENT\35433\00001\MRCPL002

APPENDIX - Item 7

IN THE UNITED STATES TAX COURT
WASHINGTON, D.C. 20217

ANDREW L. STONE	:
----------	:
Plaintiff	:
V.	:Docket No. 5311-72
	:
COMMISSIONER OF INTERNAL REVENUE	:
	:
Respondent	:

MEMORANDUM SUR ORDER

The parties have submitted separate Rule 155 computations and memoranda in support of their respective calculations in accordance with the procedure provided by Rule 155(b). The parties are in agreement as to the amount of the deficiencies in Federal income tax for petitioner's taxable years 1963, 1964, 1965 and 1966 as well as the overpayment for 1967, all determined in accordance with the findings and conclusions of the court in Jane C. Rosenbaum, et al. v. Commissioner, T.C. Memor. 1983-113. However, the parties are in dispute over the existence and amount of the overpayment of these deficiencies which petitioner contends has been made as a result of certain post notice of deficiency payments. In order to resolve the parties' dispute and enter a

Decision in this case we must decide certain legal issues. The parties' calculations are based on their opposing positions as to the proper resolution of these issues.

We must first decide whether interest on additions to tax for fraud under section 6653(b)[1/] runs from the date of notice and demand following a jeopardy assessment or from the date of notice and demand following a final decision of the Court. Many of the facts pertaining to the collection of the 1972 jeopardy assessment against petitioner have already been found by this Court in Stone v. Commissioner, T.C. Memo. 1984-187[2/] and we do not repeat them here. It is respondent's position that interest on the additions to tax for fraud for petitioner's taxable years on the additions to tax for fraud for petitioner's taxable years 1963-1964 began to run from the date of the notice and demand following the jeopardy assessments in 1972. Petitioner argues that interest

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1/
All section references are to the Internal Revenue code of 1954, as amended and in effect during the taxable years in issue.

2/
This case involved deficiencies in Federal income taxes of petitioner herein Andrew L. Stone and his wife M. Jeanne Stone for their taxable years 1972, 1973, 1974 and 1975.

has not yet begun to run because a final decision in this case has not been entered. We agree with petitioner.

Section 6601(e)(2)[3/] provides the general rule that interest does not begin to run on an assessable penalty unless it is not paid within ten days from the date of notice and demand therefor. Because petitioner filed a timely petition with the Court in the instant action, pursuant to section 6213(a) no assessment may be made until the decision of the Tax Court has become final. Thereafter, respondent may assess the deficiency and fraud penalty found by the Court to be due and the taxpayer is obligated to pay the amount assessed upon notice and demand. Section 6215(a). If the taxpayer fails to pay within the 10 day period after notice and demand, interest begins to run from the date of such notice and demand. Section 6601(e)(2). Respondent contends that such general rule does not apply in the context of a jeopardy assessment.

Prior to July 1, 1975, section 6601(b) was designated as section 6601(c) and section 6601(e) was designated as section 6601(f). For convenience, we shall refer to those subsections as they appear after June 30, 1975

In Decker v. United States, 531 F.2d 543 (Ct. Cl. 1976), the Court of Claims held that this general rule also applies where a jeopardy assessment has been made. Section 6601(b)(3) provides as follows:

> (3) Jeopardy --
>
> The last date prescribed for payment shall be determined without regard to any notice and demand for payment issued, by reason of jeopardy (as provided in chapter 70), prior to the last date otherwise prescribed for such payment.

The Court found that the proper reading of section 6601(b)(3) was that Congress intended to prevent interest from accruing by virtue of the Commissioner's use of the jeopardy assessment provisions where it would not have otherwise accrued. The court further noted that:

> If jeopardy assessments had not been made in this case, it is undisputed that payment of the 50% addition to plaintiffs' income tax liability could not have been demanded until after a final decision by the Tax Court on plaintiffs' petition. *** Accordingly, we find that it is this latter date, i.e., the date that the addition to tax would have been due in

the absence of the jeopardy assessments, that is the last date otherwise prescribed for payment of the 50% addition to plaintiffs' tax. Since the notice and demand issued to plaintiffs pursuant to the jeopardy assessments preceded the last date otherwise prescribed for payment of the 50% addition to tax, Section [6601(b)(3)] bars the IRS from assessing and collecting interest on the addition to tax. (Footnotes omitted). 531 F.2d at 546-547.

Respondent argues that Decker was incorrectly decided and contends that section 6601(b) (3) applies only in the case of a jeopardy assessment occurring prior to the last date otherwise prescribed for payment, i.e., a termination assessment under section 6851. We find this argument unpersuasive, as did the court in Decker in rejecting this narrow interpretation urged by the government in that case. The court in Decker noted that section 6601(b)(3) was a remedial statute enacted to prevent interest from accruing by virtue of the Commissioner's use of the jeopardy assessment provisions where such interest would not have otherwise accrued.[4/] Respondent's view of the statute would permit the

Commissioner not only to obtain advance payment of the additions to tax but also recover interest on the additions to which it would not otherwise be entitled. We believe such an interpretation would be a perversion of the remedial purpose of the statute.

Moreover, we believe section 6601(b)(3) is clear on its face. The statutory language itself refers specifically to "Chapter 70" of the Internal Revenue Code which includes all sections from section 6851 to 6873. Respondent's contention that section 6601(b)(3) applies only to termination assessments under section 6851 ignores the language of the statute itself and is, therefore, without merit. Therefore, because the final decision of this court has not yet been entered, no interest has begun to run on the additions to tax for fraud herein.

The Court of Claims in Motor Fuel Carriers, Inc. v. United States, 420 F.2d 702 (Ct.Cl. 1970) noted that interest does not run on the accumulated earnings tax and the sanctions for civil fraud and negligence from the due date of the return because an administrative determination must precede the imposition of such items. United States v. National Bank of Commerce, 472 U.S. 713, 720-721 (1985).

We must next decide whether interest ceased running on the portion of the deficiency equal to the account balances in two banks as of the date of respondent's levies on such accounts. In March 1972, after the jeopardy assessment was made against petitioner, respondent served notices of levy on Marine Midland Trust and the First National Bank in St. Louis, Missouri, to seize petitioner's accounts at those financial institutions. The banks did not immediately pay to respondent the account balances on the levy dates but rather remitted the amounts approximately one year later.[5/] Respondent concedes that interest on the portion of the deficiency equal to the balances in the accounts ($15,247.15 in the case of Marine Midland Trust and $44,875.50 in the case of the First National Bank) ceased to run as of the dates of the levies if we find that respondent had constructive possession of those funds as of those dates.

Marine Midland Trust remitted the account balance to the Internal Revenue Service on February 1, 1973 and the First National Bank remitted the account balance on January 15, 1973.

It is unclear whether respondent, at the time it levied on the two accounts in 1972, failed to demand surrender of the funds immediately or whether the banks simply failed to honor respondent's demand. In any event, it is clear from section 6332 that respondent had the right to require immediate surrender of the possession of such funds from the banks. See United States v. Augspurger, 81-1 USTC 9404 (USDC, W.D. N.Y. 1981). Thus, we believe respondent had constructive possession of such funds as of the date of the levies. To the extent that respondent suffered any pecuniary loss resulting from the failure of the banks to immediately honor the levies, section 6332(c) provides for a penalty against the custodian of the property. Since respondent could have immediately demanded payment of the funds and had recourse against the banks for failure to honor the demand for payment, respondent constructively received those funds prior to their actual receipt.

The United States Supreme Court has recently stated that the effect of a notice of levy is to give the Government constructive possession of such property. The Court stated:

> In the situation where a taxpayer's property is held by another, a notice of levy upon the custodian is customarily served

> pursuant to section 6332(a). This notice gives the IRS the right to all property levied upon, United States v. Eiland, 223 F.2d 118, 121 (CA4 1955), and creates a custodial relationship between the person holding the property and the IRS so that the property comes into the constructive possession of the Government. Phelps v. United States, 421 U.S. 330, 334 (1975). If the custodian honors the levy, he is "discharged from any obligation or liability to the delinquent taxpayer with respect to such property or rights to property arising from such surrender or payment." Section 6332(d). If, on the other hand, the custodian refuses to honor a levy, he incurs liability to the Government for his refusal. Section 6332(c)(1).

Thus, we find that interest ceased to run on the portion of the deficiency equal to the account balances as of the dates of the levies.

The next issue is whether a levy by respondent on an escrow account stopped the running of interest on the deficiency. Petitioner and the Department of Justice entered into an escrow agreement on July 24, 1970, whereby petitioner deposited $2,500,000 par value of short-term bonds and U.S. Treasury Bills and 21,600 shares of Concord Control, Inc. into an escrow account at St. Louis Union Trust Company. Dividends and interest received on the escrowed securities were to be deposited into petitioner's account at the

First National Bank in St. Louis. On February 8, 1972, respondent filed a notice of levy on the Trust Company instructing it to retain the principal and to hold all income it received. The income from the escrow account was placed in a separate account and it, in turn, earned interest.

In St. Louis Union Trust Co. v. United States, 617 F.2d 1293, 1294 (8th Cir. 1980), the Court of Appeals for the Eighth Circuit held that petitioner's right under the 1970 escrow agreement to receive income from the escrowed bonds and stocks was a property right subject to seizure by levy and that respondent's first levy in 1972 seized the petitioner's right to the income from the escrowed securities. In addition, this Court has ruled that petitioner did not constructively receive the income earned in the income account from 1972 through 1975. Stone v. Commissioner, T.C. Memo. 1984-187.

Respondent argues that he did not have possession of the income account until 1980 when the interpleader action brought by the St. Louis Union Trust Company was final.[9]

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[9] Petitioner's computations take into consideration the running of interest from March 15, 1976 when the interpleader action was brought until the decision therein

However, it is clear that when respondent levied on the income account in 1972, it had the right to demand immediate surrender of the funds under section 6332. Respondent chose not to do so, however, but rather instructed the trust company to retain the funds. As a result of the 1972 levy, petitioner had no access to the income account by which respondent was assured of collection of the asserted tax. There were no legal actions pending at the time of the 1972 levy to delay respondent's seizure of the funds. It is at that point that respondent constructively received the funds in the interest account. United States v. National Bank of Commerce, supra. If respondent had taken actual possession of the funds at that point, there is no question but that interest would cease running on that portion of the deficiency. The fact that respondent delayed taking actual possession of the funds at that time should not require a different result.

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was final in 1980.

The final issue[2/] presented is whether funds paid to the United States Treasury by a bank in Switzerland should be credited against the deficiency. In Rosenbaum v. Commissioner, T.C. Memo. 1983-113, we held that amounts remitted to a bank account in Switzerland (the "Agencia Account") constituted income in equal amounts to petitioner herein and petitioner in that case, Francis Rosenbaum. Petitioner recently learned, in response to a Freedom of Information Act request that the Swiss Bank paid to the United States Treasury the amounts it held on deposit, as well as shares of Alsco, Inc. stock.

Respondent does not claim that the money was not transferred to the Treasury. Rather, respondent argues that petitioner is unable to prove that such transfer occurred. While the facts are somewhat unclear on this issue, what is clear is that petitioner has made every effort to determine the whereabouts of the funds transferred out of the Swiss account. Petitioner has made a prima facie showing that the amount

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2/ Another issue concerning the effect of a 1980 settlement of a sequestration action against petitioner's wife and the resulting payment of $157,915 to respondent has been conceded by the respondent.

was paid to the United States Treasury. Respondent has introduced no evidence to rebut petitioner's evidence or to show why a payment to the United States Treasury should not be credited against petitioner's tax liabilities. Accordingly, our decision herein will be entered in accordance with petitioner's Rule 155 computation.

Richard C. Wilbur
Judge

Washington, D.C.
Dated: March 30, 1987

Supreme Court, U.S.
FILED
FEB 3 1999
CLERK

No. 98-932

In the Supreme Court of the United States

OCTOBER TERM, 1998

DOMINICK LAROSA AND CATHERINE LAROSA,
PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether equitable principles bar the United States from recovering an erroneous refund made to petitioners.

2. Whether, under the facts of this case, interest accrued on petitioners' tax liability after the date of the jeopardy assessment and seizure of their assets.

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BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. Item 2) is unofficially reported at 82 A.F.T.R.2d (RIA) 98-5257. The opinion of the district court (Pet. App. Item 3) is reported at 993 F. Supp. 907.

JURISDICTION

The judgment of the court of appeals was entered on July 10, 1998. The petition for rehearing was denied on September 8, 1998. The petition for a writ of certiorari was filed on December 7, 1998. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. On December 3, 1985, the Internal Revenue Service made a jeopardy assessment of outstanding taxes and interest against petitioners and levied on their assets (Pet. App. Item 3, at 5). Although the Service was entitled to liquidate the seized assets to satisfy the jeopardy assessment, petitioners requested that such action not be taken because they believed it would ruin their business (*id.* at 5, 27). To accommodate this concern, the government entered into an escrow agreement with petitioners that placed these assets in escrow pending the Tax Court's determination of their federal tax obligations (*id.* at 5). The escrow agreement prevented the liquidation of the assets during the pendency of the litigation and expressly provided that these assets were not to be treated as a payment of any federal tax obligation (*ibid.*). When the tax litigation was settled in 1991, the escrowed assets and the income earned on those assets were returned to petitioners (*id.* at 18).

2. The 1991 settlement was embodied in an agreed decision filed in the Tax Court (Pet. App. Item 3, at 5). Under the settlement, the parties stipulated that petitioners had underpaid their tax obligations for 1981, 1982 and 1983 and overpaid their taxes for 1984 and 1985 (*id.* at 5-6). Petitioners elected to have the overpayments (inclusive of interest) from 1984 and 1985 applied against their underpayments for 1981 through 1983. On May 1, 1991, petitioners paid the remaining balance owed (*ibid.*).

In the settlement, petitioners reserved the right to contest the amount of interest that they owed on their tax liabilities. Petitioners submitted refund claims for the interest they paid, asserting that interest should

not have accrued on their tax obligations after December 3, 1985, the date of the jeopardy assessment. That refund claim sought to recover interest in the amount of $3,694,418 (Pet. App. Item 3, at 6). Although the Service denied that claim, the Service thereafter made a refund of approximately $1.5 million for the interest that accrued between the dates on which the overpayments for 1981 and 1982 arose and the date of the final payment of tax on May 1, 1991 (*id.* at 6-7).

3. The Service subsequently determined, however, that this $1.5 million had been refunded to petitioners in error (Pet. App. Item 3, at 7). Within the time permitted by the applicable statute of limitations, the United States commenced this action to recover the erroneous refund pursuant to 26 U.S.C. 7405.[1] Petitioners asserted that the United States should be equitably estopped from recovering the refund and, in a counterclaim, sought an additional refund based upon the contention that interest on the underpayments stopped accruing on December 3, 1985, the date of the jeopardy assessment and seizure of their assets.

The district court granted summary judgment to the United States on all issues (Pet. App. Item 3, at 33). The court held that the $1.5 million refund was erroneous (*id.* at 19-22) and that the Service was not estopped from recovering that amount because "[t]here is nothing special about the case at bar in this regard" (*id.* at 25-26). The court also rejected petitioners' contention that interest should not have accrued after

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[1] Section 7405 provides that an erroneous refund "may be recovered by civil action brought in the name of the United States." 26 U.S.C. 7405. Under 26 U.S.C. 6532(b), an action for an erroneous refund is to be commenced "within 2 years after the making of such refund."

the date of the jeopardy assessment and seizure. The court held that interest continued to accrue on the underpayments after the seizure because the escrow agreement had specified that the seized assets could not be liquidated to pay the tax liabilities (*id.* at 26-30).

4. The court of appeals affirmed for the reasons set forth in the district court's opinion (Pet. App. Item 2).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. Under Section 7405 of the Internal Revenue Code, the United States is authorized to recover the amount of any tax (or interest on such tax) that has been erroneously refunded to a taxpayer. 26 U.S.C. 7405. A suit to recover such an erroneous refund may be brought at any time within two years from the date the refund is made. 26 U.S.C. 6532(b). In the present case, the United States timely sued to recover an erroneous refund of approximately $1.5 million. The courts below correctly concluded that the refund had been made erroneously (Pet. App. Item 3, at 19-24), and petitioners no longer contest that determination.

Instead, petitioners contend (Pet. 12-16) that the United States should be equitably estopped from recovering the erroneous refund simply because petitioners had not anticipated that the government would seek to recover the improper windfall that they had received. That contention has no support in the case law or governing statutes. As the courts below concluded, there is nothing about this case that takes it out of the ordinary: "it is hard to conjure a case where prior to * * * suit a taxpayer would not believe that the

IRS had acted correctly and would not make use of the refund" (Pet. App. Item 3, at 26). The plain language of Section 7405 authorizes the government "to undo such mistakes regardless of who is to blame for the error" (*ibid.*). If the sort of facts that petitioners contend creates an "estoppel" prevented the government from bringing a suit for refund, then the provisions of Section 7405 would be deprived of their natural and obvious meaning.[2]

There is no conflict among the courts of appeals on the application of equitable estoppel to suits for the recovery of erroneous refunds under Section 7405. None of the decisions cited by petitioner (Pet. 12-15) addresses that issue, and certainly no court has ever adopted petitioners' novel contention that the government may be estopped from bringing suit under Section 7405 to recover an erroneous refund of tax or interest. Further review of the decision in this case is therefore not warranted.

2. Petitioners err in claiming (Pet. 16-23) that interest was incorrectly imposed on their tax liabilities after the date of the jeopardy assessment and the seizure of their assets. The Service generally sells a

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[2] Moreover, equitable estoppel does not apply against the government on the same terms that it applies to private parties. *E.g.*, *OPM* v. *Richmond*, 496 U.S. 414, 419 (1990); *Heckler* v. *Community Health Servs.*, 467 U.S. 51, 60 (1984). When estoppel is sought against the government, the plaintiff must prove not only the traditional elements of estoppel but must, at a minimum, also show affirmative misconduct by a government employee. *Id.* at 61. No showing of any affirmative misconduct was made in this case. Moreover, the repayment of funds that should not have been received by petitioners in the first place is hardly the sort of irreparable injury that could support an estoppel against a private party, much less against the United States.

taxpayer's assets as soon as practicable after a seizure. If it fails to do so, interest on the unpaid taxes stops accruing as of the date of the seizure (to the extent that the seized assets were sufficient to satisfy the tax liability). *United States* v. *Barlow's, Inc.*, 767 F.2d 1098 (4th Cir. 1985). As the courts below correctly concluded, however, that general rule does not apply to this case.

Petitioners requested the Service not to sell the seized assets because of their concern that such a sale would ruin their business. As an accommodation to petitioners, the Service entered into an escrow agreement (i) that barred any sale of these assets during the pendency of the tax litigation and (ii) that expressly specified that the seized assets were not held as a payment of the taxes then outstanding (Pet. App. Item 3, at 5, 27). The earnings on the escrowed assets were distributed to petitioners either during the litigation or at its conclusion, when all of the escrowed assets were also returned to petitioners (*id.* at 27). It was thus petitioners, and not the Service, that received all economic benefits from the assets placed in escrow.

In these circumstances, the courts below properly concluded (Pet. App. Item 3, at 27) that petitioners' delinquent taxes could not be deemed to have been paid on the date their assets were seized and placed in escrow.[3] Interest therefore continued to accrue after the date of seizure and until the date of payment of petitioners' tax liabilities.

Petitioners err in claiming (Pet. 20) that the decision in this case conflicts with *St. Louis Union Trust Co.* v.

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[3] The district court correctly concluded that petitioners' contentions "can be restated as 'I want my cake and to eat it too.'" Pet. App. Item 3, at 27.

United States, 617 F.2d 1293 (8th Cir. 1980), supplemented by *Stone* v. *Commissioner*, 47 T.C.M. (CCH) 1502 (1984), and *Stone* v. *Commissioner*, No. 5311-72 (T.C. Mar. 30, 1987) (Memorandum Sur Order) (Pet. App. Item 7). In *St. Louis Union Trust Co.*, the court of appeals held that the Service was entitled to levy upon certain escrowed property. The Tax Court therafter held that interest on the taxpayer's liabilities stopped accruing as of the date of the levy because, following the levy, the Service had constructive possession of the assets and could have required the assets to be delivered to it. In the present case, by contrast, the escrow agreement prevented the Service from selling the assets and using the resulting proceeds to satisfy petitioners' tax underpayments. As the courts below correctly concluded, since the government was precluded from taking the steps that would have stopped the running of interest on petitioners' outstanding tax obligations, interest continued to accrue until the taxes were ultimately paid.[4]

---

[4] For these same reasons, petitioners err in relying (Pet. 19) on the prior decisions of the Fourth Circuit in *United States* v. *Eiland*, 223 F.2d 118 (1955), and *United States* v. *Barlow's, Inc.*, 767 F.2d 1098 (1985). Moreover, a conflict among the decisions of different panels of the same circuit does not warrant review by this Court. *Wisniewski* v. *United States*, 353 U.S. 901, 902 (1957).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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No. 98-932

Supreme Court, U.S.
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In The Supreme Court Of The United States

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vs.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

REPLY BRIEF OF PETITIONERS

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REPLY BRIEF FOR THE PETITIONERS

ESTOPPEL ISSUE

The Government's Brief in Opposition is -- surprisingly and tellingly -- devoid of any meaningful discussion of the conflict among the circuits on the application of estoppel against the Government.

There is good reason for this silence.

Quite apart from the obvious -- there is an irreconcilable conflict -- the Government took precisely the opposite position before this Court on the same issue ten years ago, when it was the petitioner and urged this Court to review essentially the same estoppel issue as in the case at bar.

In *Office of Personnel Management v. Richmond*, 496 U.S. 414 (1990) ("*OPM*"), the Solicitor General successfully petitioned this Court for review of the Federal Circuit's decision applying estoppel against the Government for its affirmative misconduct. 862 F. 2d 294 (Fed. Cir. 1988). The Government's Petition for Writ of Certiorari[1] (" *OPM* Petition") argued that the ruling below could not "be reconciled with this Court's prior rulings refusing . . . to estop the Government . . . ." (*OPM* Petition, at par. 7) It further justified review based on

> the absence of a clear standard for the application of estoppel to the Government [which] has led to the anomalous results like that in the present case and has prompted the development of conflicting standards among the Courts of Appeals.

(*OPM* Petition, at par. 16).

The Government did not stop there. The Solicitor General explicitly noted:

> The Court has left open the question whether "affirmative misconduct" by Government agents may in some cases justify estoppel of the Government. [Citations omitted].

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[1] Petitioners request that this Court take judicial notice of its records in *OPM*, No. 88-1943 and in particular, the Solicitor General's petition for writ of certiorari.

(*OPM* Petition, at par. 16).[2] And, the "uncertain state of the law in this area ... has generated a confusion of approaches to estoppel in the Courts of Appeals," (*Id.*, at par. 19, citing decisions in the Tenth, Eleventh, and District of Columbia Circuits.) Those cases, the Solicitor General admitted, declare that estoppel against the Government may "be appropriate under certain circumstances," *Id.*, at par. 20. Certiorari was granted.

On the merits, this Court painstakingly surveyed the array of contradictory, inconsistent rules which the lower courts had developed, some in reliance on language from this Court's own prior opinions.

> [D]icta in our more recent cases have suggested the possibility that there might be some situation in which estoppel against the Government could be appropriate.

496 U.S. 417, 421. And, the lower courts had seen "numerous claims for equitable estoppel" *Id.*, at 422, due to the "inadequate guidance for the federal courts . . ." *Id.*, at

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[2] Not one of the traditional dangers of estoppel against the Government -- cited by the Government in its petition in *OPM* -- is present here. Estoppel will not result in what the law "does not sanction or permit." *OPM* Petition at par. 8-9, quoting *Utah Power and Light Co. v. United States,* 243 U.S. 389, 409 (1917); nor "give the words of the Executive Branch officials the force of law, while suspending implementation of the conditions established by Congress." *Ibid;* nor "force the expenditure of public funds contrary to the express mandate of Congress," *OPM* Petition at par. 11.

422-423. This Court concluded, "We leave to another day whether an estoppel claim could ever succeed against the Government." *Id.*, at 423.

That "other day" has come; the hodgepodge of contradictory and inconsistent rules justifies review here.

What, then, have become of the "absence of a clear standard," the "conflicting standards," the "shar[p]" conflict, and the "confusion of approaches to estoppel" that the Government clearly perceived in *OPM* and that prompted this Court to grant review in *OPM*? Suddenly, in this case where the Government won below, such conflicts have magically disappeared. But they have not.

To the contrary, yet more cases reflect the conflict. *In re DePaola*, 45 F. 3d 373, 377 (10th Cir. 1995) (IRS may be estopped by a showing of affirmative misconduct as well as the traditional elements of estoppel); *Linkous v. United States*, 142 F. 3rd 271 (5th Cir. 1998) (Estoppel available for affirmative misconduct and the traditional elements of estoppel).[3]

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[3] *Mendrala v. Crown Mortgage Co.*, 955 F. 2d 1132 (7th Cir. 1992); *Bolt v. United States*, 944 F. 2d 603, 609 (9th Cir. 1991) ("Affirmative misconduct (not mere negligence) and a serious injustice outweighing the damage to the public interest . . . .")

Therefore, guidance is sorely needed to resolve this jungle of inconsistent, conflicting rules.[4]

It is no response to argue that no conflict exists "on the application of equitable estoppel to suits for the recovery of erroneous refunds under Section 7405," (Brief in Opposition. at par. 5). The particular government remedy is not the issue, but rather whether the Government may be estopped by its actions in the first place from any recovery, no matter what the vehicle. Section 7405 is simply one of several procedural mechanisms for the Government to recover funds where it believes it has made a mistake. Others (among many) include a suit to reduce an assessment to judgment (Code §§7401, 7402), a suit to foreclose a tax lien (Code §7403) or a suit to collect estate taxes (Code §7404).

Any impact that application of estoppel may have on Code §7405 simply highlights why this case is even more important and more worthy of this Court's review.

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[4] Footnote 2 of the Brief in Opposition misstates the holding in *OPM* and another case. This court has never stated an estoppel rule of general application, but if affirmative misconduct is a requirement, that misconduct is demonstrated by the uncontradicted record here -- the highest ranking official of the Petitioners' IRS district apologized in writing to him for delaying his refunds, told him he was entitled to refunds, and wrote "Mr. LaPosa will receive refund checks ... in a few weeks." Petition for Writ of Certiorari, Appendix - Item 5. *In re DePaolo*, 45 F. 3d 373 (Affirmative misconduct "means an affirmative act or misrepresentation or concealment of a material fact." *Id.*, 377)

Taxpayers who rely on the IRS grant of a refund and spend it (as the District Court thought would always be the case (Brief in Opposition, 4-5)) would feel secure against later allegation of IRS error. Others who invest or save their refunds could not invoke estoppel because they had not detrimentally relied on the correctness of the refund. (This is in contrast to the right of the Government to audit a tax return and collect the additional taxes, even after a refund, a circumstance which by definition is created by a taxpayer error.)

DUTY TO STOP RUNNING OF INTEREST

The Petition cited ample authority for the IRS' legal duty to apply monies it seizes to taxes it assesses, and to do so right away. Nor has the Government ever disputed that general duty. The Government "held and hit" the taxpayers: The IRS would not release their funds, would not apply them to pay the taxes, and as a result, interest on the taxes on the penalties, and on the interest, continued to accrue and be compounded daily.[5]

The Brief in Opposition conveniently ignores the uncontradicted and undisputed fact that the "escrow" was not even in place for 44 days following the jeopardy

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[5] In stark contrast to the Brief in Opposition's "cake" metaphor, the fact is that these taxpayers suffered the worst possible outcome because the escrow was forced on them. See p. 8-10 below.

assessment. Thus, the Government's factual assertions regarding the escrow, even if correct, are irrelevant. First comes the issue of the IRS' duty on Day 1 after the levy. Since that duty is clear and undisputed, the inquiry should stop there. The Fourth Circuit's sanction of the IRS' failure to credit the seized cash against the assessed taxes while no escrow was in existence conflicts with long-standing precedent in the Courts of Appeals, in this Court, and in statute. Petition for Writ of Certiorari, 16-23.

The Government further argues that this case is not certworthy solely because of the escrow and attempts to distinguish *St. Louis Trust Co. v. United States*, 617 F. 2d 1293 (8th Cir., 1980), supplemented by *Stone v. Commissioner*, 47 TCM (CCH) 1502 (1984), and *Stone v. Commissioner,* 5311-72 (TC March 30, 1987) (Memorandum Sur Order). That attempt is in error. *St. Louis Trust Co.* and its follow-on cases hold that interest on a tax liability stops the day the Government seizes assets, even assets in escrow, because the IRS' levy puts it in constructive possession of the cash.[6]

It is no answer to say that the escrow "prevented the Service from selling the assets." First, there were no

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[6] Indeed, in this case the Government actually received one payment, for $282,000, and in fact applied it to the taxes just as the law requires for the remainder.

saleable "assets" involved, only cash and cash equivalents. Second, the escrow did not even exist for 44 days after the seizure. The Brief in Opposition would have this Court ignore that inconvenient fact.

RESPONSE TO GOVERNMENT'S INCORRECT DESCRIPTION OF FACTS

We believe the discussion above sufficiently addresses the legal points raised by the Brief in Opposition. However, we cannot allow several serious factual errors in that brief to go unanswered, facts important to the Petitioners' request for review.

By relegating to subordinate clauses the very issues sought to be reviewed, the Government's opposition seeks to obscure and gloss over the principal issues in the case. Moreover, the low-key, casual, clinical tone of the Brief in Opposition tries to lull this Court into a false impression of the seriousness of the fights that have consumed these taxpayers for nearly 15 years. Theirs was no gentle, reasonable dispute among mutually-respecting parties. It was a knock-down, drag-out battle with heavy casualties -- all on the taxpayers' side. The jeopardy assessment resulted in placing $20 million of cash and non-cash property in the hands of the Government. Then the taxpayers appealed these assessments and lost. *LaRosa vs. United States,* 841 F. 2d 544 (4th Cir. 1988). Then the Government was paid more money in the Tax Court settlement. The taxpayers asked for some of the interest

back. Forced to confront the issue by Congresswoman Morella, the IRS admitted its a mistake and refunded $1.5 million to the taxpayers. Then it sued to get that back, plus interest. The dispute was and is bitter.

Petitioners never "requested" that the Government not liquidate their assets to satisfy the jeopardy assessment (Brief in Opposition at 2, par. 1), and never "requested" the Service not to sell the seized assets because of their concern that such a sale would ruin their business. *Id.*, at 6. The escrow was not "an accommodation to the Petitioners,...".

These contentions are untrue, and unsupported in the uncontradicted record. To the extent the Government's opposition depends on them, it must fail. For example, in Petitioners' 1991 Tax Court settlement, approved by a representative of the Chief Counsel of the Internal Revenue Service, the Tax Court held, among other things, that under the escrow and jeopardy assessments, "access to and use of [Petitioners'] money effectively has been restricted and extremely costly to the LaRosas for over four years." (Appendix, Item 9, *infra*) Further, "with the release of all of their funds, the LaRosas will restart their previously successful coal business in West Virginia,..." Thus, it was clear -- and agreed to by the IRS -- that putting the Petitioners' money in escrow had stopped, not preserved, the LaRosas' coal business.

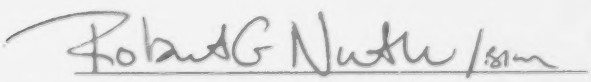
Moreover, the LaRosas submitted ample evidence below in support of their well-pleaded allegations that the "escrow" was coerced and therefore invalid. We urge this Court to consider the sworn declarations of the LaRosa brothers, excerpts from which are in the Appendix (Items 8, 10, 11) in further support of this contention.

In correcting the record, the Petitioners wish to alert the Court that this escrow arrangement was not a voluntary, mutually agreeable, happy "accommodation" among two respectfully disagreeing parties. It was an illegal, coerced contract of adhesion that was invalid because it was not the product of mutual agreement.

CONCLUSION

For the foregoing reasons, the Petition for Writ of Certiorari should be granted.

Respectfully submitted,



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APPENDIX - Item 8

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND
Southern Division

UNITED STATES OF AMERICA,	*	
	*	
Plaintiff,	*	
	*	
v.	*	CIVIL ACTION
	*	NO. 96-980
	*	
DOMINICK LAROSA	*	
and	*	
CATHERINE LAROSA,	*	
	*	
Defendants.	*	

DECLARATION OF DOMINICK LAROSA

Dominick LaRosa, under the penalties of perjury, declares as follows:

1. I am an individual residing in Maryland. I am making this Declaration to explain some of the circumstances under which the assets of my brother, myself and my wife Catherine, and our corporation, were placed in escrow by the Internal Revenue Service.

2. During the 1970s, my brother Joseph LaRosa, my father Pietro LaRosa, and I worked in coal mines in West Virginia. Together, we built up a substantial

business, mostly supplying coal to utility companies from West Virginia mines.

3. Our company was called The LaRosas International Fuel Company, which was a Maryland corporation. The comptroller of the corporation was my brother, Joseph LaRosa. He has detailed knowledge of the finances of the corporation, as well as of its tax matters. He is supplying a separate declaration to describe many of the issues involved in this tax refund and erroneous refund suit. I would like to supply some details as to how an escrow agreement involving all of our assets operated.

4. Some time in 1984, the Internal Revenue Service began an examination of the corporation's federal income tax returns and liabilities. This examination also included my tax returns and those of Joseph.

5. The IRS eventually determined that the corporation had understated income for certain years and overstated income for other years. As a result, the IRS made adjustments to the corporation's income, and these adjustments flowed through to myself and my brother on our personal income tax returns.

6. On or about December 3, 1985, the Internal Revenue Service made jeopardy assessments against the corporation, as well as against me (and my wife, Catherine) and my brother, Joseph. The total amount of these assessments was over $20 million, but these were eventually reduced to about $3.4 million in tax, $2.5

million in penalty, and $4.0 million in interest (due to the delay in entering the settlement until May, 1991) as a result of an action to contest the assessments in the United States Tax Court.

7. To collect the jeopardy assessments, the Internal Revenue Service levied on property belonging to the corporation and to my family. A complete list of the property that was seized is contained as an exhibit to this declaration.

8. The cash and cash equivalent amounts of funds seized was in excess of $12 million. Of this, $282,669 was actually paid over to the IRS by more than one bank before the escrow was put in place. In addition, substantial other properties were also seized. The total of other, non-cash properties seized was substantially more than $8 million in fair market value.

9. The IRS representatives told us that if we did not agree to the escrow, they would simply liquidate everything else and pay the jeopardy assessments. Of course, that would mean our business was ruined. Faced with this choice, we reluctantly signed on to using the escrow device. The escrow language was entirely the product of the IRS and its attorneys. My attorney proposed many changes, but these were all refused. Among other things, I wanted access to the principal in order to run my business, but this was rejected. This escrow was under threat and under duress. It was the only way the IRS would

agree not to sell everything. The IRS agreed only to very minimal payments, and those from the interest only, toward living expenses. Only about 3% of the income was paid in this way.

10. After these levies, the IRS did not immediately apply the levied property (cash and non-cash) to pay the jeopardy assessments (except for the $286,889). On January 16, 1986, an escrow agreement was entered into. A copy of that escrow agreement is attached to this declaration as Exhibit 1. Pursuant to the escrow agreement, the remaining property which had been levied upon, including particularly the cash and cash-equivalents, was placed in escrow pending the outcome of the Tax Court case described below.

11. We retained counsel to contest the jeopardy assessments. In addition, the IRS sent statutory notices of deficiency to myself and my wife, Catherine, to Joseph, and to the corporation. Our lawyers contested these statutory notices by filing petitions in the United States Tax Court.

12. It took about five years for these Tax Court petitions to be resolved, and they were finally settled in May, 1991.

13. During all of that time, and indeed since January 16, 1986, that is, for five and one-half years, the property described above remained in escrow.

14. Neither I nor my brother had any authority to control the escrowed property. We had to ask the Internal

Revenue Service for money to pay many expenses. These included utilities, gas, auto insurance, school tuition and other items. Any item that was allowed to be paid was allowed only in a grudging way, and after much debate and consideration. Many times these payments were late. I received only a few thousand dollars per month, which was based on the necessities that the IRS said were allowed to be paid. This was much less than the amount earned on those escrowed funds. Even those small payments were sometimes a problem being "approved" by the IRS agent in charge of the escrow.

15. We of course had to pay federal tax on the income that was earned from the escrowed funds, but we were given only enough money to pay these taxes, not the income on which tax was charged. However, we also had to file Maryland State income tax returns, which also had to reflect the income from the escrowed funds as gross income for Maryland State tax purposes. Here, however, the Internal Revenue Service refused to give us any funds to pay our state income taxes until the Tax Court cases were settled in 1991. As a result, we incurred substantial interests and penalty charges for 5 ½ years on these underpaid taxes.

16. The other aspect of the escrow agreement was the principal, as contrasted with the income. There was absolutely no question that the Internal Revenue Service refused at all times to release the principal of the

escrow. So, while at some points the IRS allowed a small portion of the income to be paid to us (to cover living expenses), at no time did the IRS ever allow any of the principal to be released (until the Tax Court cases were settled), and the IRS refused requests to release that principal. Thus, we had no control over the principal of the escrow.

17. At one time, I recall asking for a release of funds so that we could buy another coal business. By our calculations, we demonstrated that even paying that amount would still have left enough for the IRS, but this request was refused.

18. For all of these and other reasons, I did not have unfettered control, or indeed any control, over either the principal (or the income) from the escrowed properties.

Under penalties of perjury, I declare that I have examined the foregoing statement of facts in the foregoing Declaration, and to the best of my knowledge and belief, it is true, correct, and complete.

April 6, 1997 /s/ Dominick LaRosa
Date

APPENDIX - Item 9

UNITED STATES TAX COURT

DOMINICK LAROSA and LORETTA LAROSA,	)	
Petitioners,	)	Docket No. 6171-86
v.	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

DECISION

Pursuant to the agreement of the parties in the above-entitled case, it is:

ORDERED AND DECIDED: That the following statement shows the deficiencies in income taxes and additions to taxes due from the petitioners for the taxable years 1981, 1982 and 1983 without taking into consideration the jeopardy assessments made on December 3, 1985:

1981

Deficiency in income tax, without taking into consideration the jeopardy assessment made on December 3, 1985: $284,407.00

Payments/Refunds	
12/17/85	721.00
12/17/85	23,474.00
04/07/87	<23,474.00>
Total Payments	$ 721.00
Deficiency (to be paid)	$283,686.00

That there is an addition to tax due from the petitioners for the taxable year 1981, under the provisions of I.R.C. §6653(b) in the amount of $85,322.00.

1982

That there is a deficiency in income tax due from the petitioners for the taxable year 1982, in the amount of $820,787.00.

That there is an addition to tax due from the petitioners for the taxable year 1982, under the provisions of I.R.C. §6653(b)(1), in the amount of $246,236.00.

That there is an addition to tax due from the petitioners for the taxable year 1982 under the provisions of I.R.C. §6653(b)(2), equal to 30 percent of the statutory interest due on $770,376.00 from April 15, 1983 to December 3, 1985.

That there is an addition to tax due from the petitioners for the taxable year 1982, under the provisions of I.R.C. §6661, in the amount of $82,079.00.

1983

That there is a deficiency in income tax due from the petitioners for the taxable year 1983, in the amount of $468,081.00.

That there is an addition to tax due from the petitioners for the taxable year 1982, under the provisions of I.R.C. §6653(b)(1), in the amount of $140,424.00.

That there is an addition to tax due from the petitioners for the taxable year 1982 under the provisions of I.R.C. §6653(b)(2), equal to 30 percent of the statutory interest due on $1,060,555.00 from April 15, 1984 to December 3, 1985.

That there is an addition to tax due from the petitioners for the taxable year 1982, under the provisions of I.R.C. §6661, in the amount of $46,808.00.

Judge Entered:

* * * *

It is stipulated that the Court may enter the foregoing decision.

In settling this case with the Internal Revenue Service (hereinafter, "IRS"), the taxpayers, Dominick LaRosa, Joseph LaRosa, and the LaRosa's International Fuel Co., Inc., (hereinafter, collectively, "the LaRosas"), reaffirm and reiterate that their federal income tax returns for the taxable years 1979 through 1983, the years covered

by the Settlement Agreement, were filed correctly and properly under federal and state tax law.

The LaRosas are settling this case for the reasons stated in this settlement memorandum and specifically reserve all rights open to them to appeal or to otherwise contest their tax liability with the State of Maryland (hereinafter, "Maryland"), including their right to apply for a pardon from Maryland.

In settling this case with the IRS, the LaRosas state that they have committed no wrong in filing their federal and state income tax returns for the years covered by the Settlement Agreement, 1979 through 1983. The LaRosas deny committing any act or omitting any income that would cause any addition to tax under the Internal Revenue Code (hereinafter, the "Code"). The LaRosas enter into this Settlement Agreement for the sole and only purpose of finally disposing of these United States Tax Court cases with the IRS.

The LaRosas maintain that their company intended to file and did file its 1979 and subsequent year federal and state corporate income tax returns and reported the income from the contracts involved in these cases on the completed contract method of accounting (hereinafter, "CCMA"). The LaRosas maintain that in 1979 when they obtained their first contracts that they kept their books on the CCMA. The LaRosas maintain that all the contracts involved in these cases consist of long-term contracts. The

LaRosas maintain their company filed an election on its 1979 federal income tax return electing and advising the IRS that it was electing CCMA. The company's originally filed 1979 federal income tax return has been lost by the IRS. The LaRosas maintain their company was entitled to use the CCMA from 1979 through 1985 in reporting the income from the contracts involved in this case. The LaRosas and their company maintain they properly and timely filed, timely reported, and timely paid tax upon all the income from the contracts.

The LaRosas have agreed to settle for the following reasons;

First, to try and possibly appeal this case would be a lengthy and costly process. This case probably would not be decided by the Tax Court for at least twelve (12) months or longer. The LaRosas also recognize the substantial possibility that the IRS would appeal any verdict unfavorable to the IRS, and appeal process which would probably consume more than a year. Thus, even when the LaRosas secure the favorable verdict, which they fully expect, the trial and appeal is expected to continue for more than two (2) years from the trial date.

Second, settlement will release all the money to them which the IRS has held under jeopardy assessments for over four (4) years. While the LaRosas maintained upon assessment, and continue to maintain, that the jeopardy assessments were improper, the reality is that

access to and use of their money effectively has been restricted and extremely costly to the LaRosas for over four (4) years.

With the release of all of their funds, the LaRosas will restart their previously successful coal business in West Virginia, thereby employing several hundred currently unemployed workers and producing substantial revenues for the federal and state governments. Moreover, a prompt release of the money currently levied against by the IRS is essential to securing several lucrative coal supply contracts which must be bid on within the next several months. Prominent individuals concerned with the West Virginia's and Maryland's economies have implored the LaRosas to settle with the IRS so that they could restart their coal business and bring an immediate economic benefit to the various governments.

Third, the LaRosas recognize the inherent litigation risk in proceeding with a trial, even though they and their legal counsel believe their case is totally meritorious and that they would win.

Fourth, the LaRosas' tax advisors have advised them that settlement would enhance their tax planning capability for the taxable year 1990.

Fifth, the emotional toll on the LaRosas and their families has been devastating, and they want to end this nightmare of almost five years duration. For example, the LaRosas' parents are elderly and are experiencing health

problems which normally affect their age group. The LaRosas recognize their parents' anguish over this case and believe that settlement is necessary to remove this parental concern and potential health detriment. Additionally, the strain on the wives of Dominick and Joseph LaRosa is acute, and Dominick LaRosa recognizes that his children have been and will continue to be adversely affected by protracted litigation.

Finally, the LaRosas believe that this settlement establishes the principle and demonstrates what they have always advanced with the state and the IRS -- that as taxpayers they were always, and are willing to pay their proper and fair share of taxes to the federal and state government.

That the petitioners waive all litigation costs incurred in this proceeding pursuant to the provisions of I.R.C. §7430.

It is stipulated that the petitioners have reserved the right to pursue an action in the appropriate federal court with respect to the interest claimed to be due by the I.R.S. on the respective deficiencies.

Abraham N. M. Shashy, Jr.
Chief Counsel
Internal Revenue Service

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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND
Southern Division

UNITED STATES OF AMERICA,	*	
	*	
Plaintiff,	*	
	*	
v.	*	CIVIL ACTION
	*	NO. 96-980
	*	
DOMINICK LAROSA	*	
and	*	
CATHERINE LAROSA,	*	
	*	
Defendants.	*	

DECLARATION OF JOSEPH LAROSA

Joseph LaRosa, under the penalties of perjury, declares as follows:

1. I am an individual and a resident of the State of Maryland. I am making this Declaration to tell the Court some of the circumstances under which my brother, Dominick LaRosa, received the tax refunds at issue in this case.

2. I was (and remain) the Comptroller of the Corporation. In that capacity, I have personal knowledge of

its operations. This knowledge includes monitoring its receipts and disbursements, its tax payments and liabilities, and other aspects of its finances. Because of the IRS audit described below, I also came to have knowledge of Dominick LaRosa's personal finances, including his tax payments to the IRS over the years from 1981 to the present. I have also examined IRS transcripts of account, specifically the account transcripts relating to Dominick, the Corporation and myself. Finally, I was in charge of monitoring the tax aspects of the Tax Court settlement described below, assisting our attorney at the time. I also monitored, through my own calculations, the taxes, penalties and interest charged by the IRS and reflected in the claim for refund.

3. My brother, Dominick LaRosa, and his wife, Loretta Catherine LaRosa, also reside in Maryland. They are the Defendants in the above-captioned action.

4. During the 1970s, my brother, Dominick LaRosa, and my father, Pietro LaRosa, and I worked in coal mines in West Virginia. Together, we built a substantial business to supply coal from West Virginia mines to utility companies.

5. Our work was performed through a corporation, The LaRosas International Fuel Company. This was a Maryland corporation owned by my brother, Dominick, my father, and myself.

6. Over the years, and through the late 1970s and early 1980s, the corporation gained many contracts with utility companies that involved many millions of dollars of sales.

7. Shortly before December 3, 1985, the Internal Revenue Service formally opened an income tax examination of the corporation's federal income tax returns and liabilities. The years under examination for the corporation were 1979 - 1983.

8. The IRS also opened income tax examinations of myself and my brother, Dominick. The years under examination were 1981 - 1983.

9. As I describe more fully below, the Internal Revenue Service determined that the corporation had understated its income for certain years (the earlier years) and overstated income for other years. The resulting understatements and overstatements of income were then attributed to myself, personally, as well as to my brother, Dominick and his wife Catherine.

10. On December 3, 1985, the Internal Revenue Service made jeopardy assessments against the corporation, as well as against Dominick and Catherine, and myself. The total amount of these jeopardy assessments was in excess of $20 million. Eventually, as I explain below, these amounts were reduced to about $9 million (including penalty and interest), as a result of a settlement in the United States Tax Court.

11. To collect the jeopardy assessments, the IRS levied on property belonging to my family and to the corporation. A complete list of the property levied upon is contained in Exhibit 1. (This list is also an exhibit to the declaration of Dominick LaRosa.)

12. The fair market value of the property levied upon was in excess of the amounts eventually determined to be due under the Tax Court settlement that we eventually filed to contest the jeopardy assessments. The approximate value of the cash and cash-equivalent property was $12 million. That property, if applied to Dominick and Catherine's taxes and that of myself and the corporation, would have fully paid those taxes as eventually and finally determined by the Tax Court. (Other non-cash property was also seized.)

13. After the December 3, 1985 levies, the Internal Revenue Service did not immediately apply the levied property to pay the jeopardy assessments. On January 16, 1986, an escrow agreement was entered into. A copy of this escrow agreement, together with a list of the escrowed property, is attached as Exhibit 1. Pursuant to the escrow agreement, property which had been levied upon was placed in escrow pending the outcome of the Tax Court case.

14. The family retained counsel to contest the jeopardy assessments. Pursuant to Section 7429 of the Internal Revenue Code, a Complaint was filed in the United

States District Court for the District of Maryland seeking to contest the reasonableness of the jeopardy assessments. After a hearing, the Federal District Court found that the making of the assessments was "reasonable" and dismissed the Complaint. The dismissal of the Complaint was upheld on appeal.

15. Following the jeopardy assessments, the Internal Revenue Service also issued formal notices of deficiency, which I have learned are required by law.

16. These notices of deficiency describe the process by which a taxpayer is allowed to contest the assessments in the United States Tax Court by filing a Petition.

17. Through our attorneys, Dominick and Catherine, the corporation and I filed Petitions with the United States Tax Court to contest those notices of deficiency.

18. On or about May 1, 1991, more than five years after the jeopardy assessments, these Tax Court cases were settled. I have attached as Exhibits 2,3 and 4, copies of the formal settlement papers. These decisions provided that, during the years 1979 - 1983, the corporation, Dominick and Catherine and I were liable for amounts totaling $4,972,507 of income tax and penalties, as set forth below. It is to be noted that the settlements, by their terms, were just that -- settlements.

[Table Omitted]

* * * *

42. Paragraphs 10-13 above describe the fact that our family's property was placed in an escrow account for 5-1/2 years, while the Tax Court case was pending. However, even though the escrow agreement was signed in January 1986, it was by no means a voluntary act.

43. At that point, the Internal Revenue Service had seized all of the family's liquid assets and all of our business assets. Because of these seizures, we had absolutely no way to run our business, and we stood to default on multi-million dollar contracts.

44. Internal Revenue Service representatives told us in no uncertain terms that the escrow option was available, but that if we did not "agree" to it they would simply liquidate everything they could and pay the jeopardy assessments. They had already seized and applied $282,669. That, of course, would have meant the ruin of our business that we had spent so much time to develop.

45. Accordingly, under the duress and threat of a ruined business enterprise, we were forced to sign the escrow agreement. It was not voluntary on our part. It was the only way the IRS would agree not to liquidate all the assets it had seized.

46. The operation of the escrow agreement showed that the Internal Revenue Service had complete control over the funds. First, at no time during the life of that agreement were we ever permitted to have access to the principal of the agreement. At most, and under difficult circumstances, the IRS permitted certain amounts from income to be paid for living expenses. But this in no way affected the fact that the IRS, from the time of the seizures, had complete and unfettered possession of the corpus of the escrow agreement. Under no circumstances would the IRS agree to release the corpus. Only on May 14, 1991 was the escrow finally released. Exhibit 13.

47. During the course of this agreement, Dominick and Catherine needed funds for many different purposes. School for the children was necessary, the payment of state income taxes was necessary, and many other expenses were necessary to be paid from the income from the escrow agreement. On many occasions he and I asked the Internal Revenue Service to release funds. In almost every case they were slow to release the funds or they were late releasing the funds. The result was in embarrassment and monetary penalties on the part of our creditors. In fact, until the end of the escrow, the IRS would not even release money to pay the Maryland State income taxes due on the income from the escrowed assets. As a result, we incurred substantial penalties and interest from

the State of Maryland, and were forced to spend considerable legal fees.

48. For these and other reasons, Dominick and Catherine did not consider that they had unfettered control, or any control, over either the principal or the income from this escrow agreement.

49. Since we had no control over the escrowed amount or the income from it, all of which was subject to the IRS' "veto" according to the terms of the escrow agreement, we could not devote the principal or the income from the agreement to other purposes. Those purposes would have included the expansion and operation of our business. Without those funds, the corporation today is a much smaller enterprise and far less profitable than it could have been had we been able to invest the principal that belonged to us.

50. During the course of the events described above, I had occasion to prepare computations relating to the claim for refund filed by our attorneys after the Tax Court settlement. In these computations, which are attached as Exhibit 14, I calculated how much interest the IRS charged (per federal tax interest rates on underpayments) from December 3, 1985 through the dates that Dominick LaRosa was given his two refunds in 1994. Under the claim for refund, that interest should not have been charged, and so when the claim was prepared, that was the amount of interest that was claimed as being due to

Dominick (plus interest). The chart below summarizes that computation, and also sets out the actual refunds which Dominick received as offsets. The differences are the amounts that should be refunded in this lawsuit (plus interest):

[Table Omitted]

51. I declare, under the penalties, that I have examined the foregoing Statement of Facts and the foregoing Declaration, and to the best of my knowledge and belief it is true, correct and complete.

April 6, 1997
Date

/s/ Joseph LaRosa

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND
Southern Division

UNITED STATES OF AMERICA,	*	
	*	
Plaintiff,	*	
	*	
v.	*	CIVIL ACTION
	*	NO. 96-980
	*	
DOMINICK LAROSA	*	
and	*	
CATHERINE LAROSA,	*	
	*	
Defendants.	*	

SECOND DECLARATION OF DOMINICK LAROSA

Dominick LaRosa, under the penalties of perjury and pursuant to 28 U.S.C. Section 1746, declares as follows.

1. I am a defendant and counter claimant in the above-entitled case, and I am making this second declaration to further explain some of the circumstances surrounding the creation of the escrow agreement at issue in this lawsuit.

2. First, some background is necessary. The LaRosa's International Fuel Company, Inc., which was run by myself, my brother Joseph, and my father Pietro during

the 1980s, was advised to use the long-term completed contract method of accounting in order to account for long-term contracts we had negotiated. These were with major utilities that used coal for their electric generating operations. The most important of these utilities was the Allegheny Power Systems. This method was selected upon the professional advice of our accountants. Since the contracts were due to be completed by the end of 1985, we were advised and were prepared to report all of the income from these contracts in our 1984-1985 taxable years. This method of accounting for long-term contracts, we were advised, is fully sanctioned by the Internal Revenue Code. It meant that the income from the contracts would not have to be reported in the early years (1981-1983), but only in the later years of the contract. It was for this reason that there were reported large amounts of money in 1984-85 and lesser amounts in 1981-83.

3. The Internal Revenue Service's levy on December 3, 1985, upset our entire plans for the Corporation, to say the least. About forty-five days after these jeopardy levies, seeing that our business was totally shut down and all of our assets were seized (business and personal), an escrow agreement was entered into involving the assets that were seized.

4. Under no circumstances could this escrow be considered one that I "agreed to" voluntarily. It was forced on us and coerced by the IRS. The IRS had seized

all of my and my corporation's liquid and non-liquid assets. By that act, the IRS completely deprived me, my brother, my father and the corporation of the ability to do business. The IRS had even seized our cars, business equipment and other items of property. The Corporation and I faced total economic ruin if we did not "agree" to the escrow.

5. The so-called "agreement" to form the escrow was not an act of free will. It was not a matter of choice. If we did not "agree" to it, the IRS insisted it would liquidate everything -- that is, all of the property and money -- and apply these to the $20 million of assessments it had made, assessments which were later settled at less than half of the original amount. The IRS ended up keeping the property in escrow for 5-1/2 years.

6. I have also read the motion papers of the United States in this matter, wherein it contends that the refunds it issued to me and my wife in 1994 were in error. While I understand that this is the position the Government takes today, it certainly was not what the IRS said in 1994 when the refunds were issued. In fact, when I applied for these refunds, not only did the IRS believe the refunds were warranted because it had charged too much interest on the original taxes, but the IRS also apologized to me for the inconvenience it caused by keeping all of the money as long as it had. A copy of the letter I received from the IRS (and which was addressed to my Congressperson, Ms. Morella)

is attached to this Declaration as Exhibit 1. This letter reads in part as follows:

> We are sorry that Mr. LaRosa's dealing with the Internal Revenue Service have [sic] been less than satisfactory. Please be assured that we share your concern that all taxpayers receive efficient and courteous treatment....Please extend our apology to Mr. LaRosa for any inconvenience this may have caused.
>
> I have been told, and I understand, that legally the United States can still ask for the refunds back in this lawsuit despite this letter, but in 1994 when the refunds were issued both I and the IRS believed they were correct.

7. So, not only did the IRS make a jeopardy assessment against me in 1985, but in the end, it was settled for less than half of the original jeopardy assessment. When, through my lawyers, I applied for a refund of interest, it took the IRS another three years to grant that refund (apologizing for the inconvenience it "may" have caused -- an understatement if there ever was one). To add insult to injury, two years after that it has sued me to get that refund back, and claims interest on top of that!

8. I have also read the Plaintiff's Reply concerning the operation of the escrow account. The statements in that legal brief do not appear to be verified by any declaration, and in some respects, they are completely wrong. For example, my brother Joseph and I were not

given $20,000 per quarter as it suggests, but only about $9,000 per quarter, or $36,000 per year for certain living expenses. Second, all of the other expense categories noted in the Plaintiff's brief were normal expenses of living, including what is called "private school tuition" which included college tuition for my daughter. The oil and gas investment was a legally binding contract that was entered into before the jeopardy assessments, so the IRS apparently agreed to pay this. This was to protect the IRS in any event, because these investments were very valuable at the time.

9. The legal and accounting fees category was almost solely the result of the IRS' jeopardy assessments, and the efforts my family had to expend to settle the Tax Court litigation and fight the jeopardy assessment case. These expenses would not have been incurred if the IRS had not made their jeopardy assessments.

10. It is a misstatement that our corporation and business kept going while the 5-1/2 years of the Tax Court litigation continued. The fact that the IRS had tied up all of my family's assets by way of the escrow meant that we could not operate the business, and it remained in a dormant state for those years, and after. It remains largely dormant today, though I am trying to revive it. To claim, as the Plaintiff's brief does, that the business did so well that we could write a check for $3.6 million in 1991 is also wrong. In fact, we could not. In fact, the $3.6 million

check was issued by the Corporation after that amount of money was transferred from the escrow to the Corporation at the conclusion of the Tax Court litigation. Specifically, at the time it was agreed to transfer the cash from the Corporation's account with American Capital Financial Services, Inc., where the Corporation had more than the $3.6 million (in escrow) in the American Capital Government Securities Fund. This source is noted in my brother Joseph LaRosa's Declaration, specifically at Exhibit 1, on the 6th page following the escrow agreement.

11. Even though the Plaintiff's Reply brief is not verified on the subject if the disbursements from the escrow, and is factually incorrect, it is also incomplete. For example, it does not state the fact that in many cases, the IRS failed to allow payment of many personal expenses, or where it did, they were late. The insurance payments were often late because of the IRS. The electric and gas bills were often late, with cutoff notices coming to my home for the first time in my life. On top of this, the IRS' jeopardy assessment caused the Corporation to lose the renewal of its contract with Allegheny Power Systems. That contract could have lasted for up to 30 years, with hundreds of millions of dollars in sales. There were other items detailed in my previous declaration which were not paid or not paid timely.

12. At no time did the IRS ever agree to let my family have access to the principal of the escrow. As noted,

the only access we had to the interest in part, and even that access was grudgingly given.

13. The United States apparently has possession of the checks from the escrow account. I do not. I have not had an opportunity to review all of the escrow checks since these have not been provided to me in this litigation. Thus, I cannot fully determine whether the statements made in the government's brief, even if they were verified, are otherwise be true.

* * * *

5/7/97

Date /s/ Dominick LaRosa